

New York State

Economic Report

February 2006

**Sheldon Silver
Speaker**



**Herman D. Farrell, Jr.
Chairman**

**New York State Assembly
Ways and Means Committee Staff**

NEW YORK STATE
ECONOMIC REPORT

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Chairman
Assembly Ways and Means Committee

Prepared by the
Assembly Ways and Means Committee Staff

February 27, 2006

Dear Colleagues:

I am pleased to provide you with the New York State Assembly Ways and Means Committee's Economic Report for 2006. This report continues our commitment to providing clear and accurate information to the public by offering complete and detailed assessments of the national and State economies.

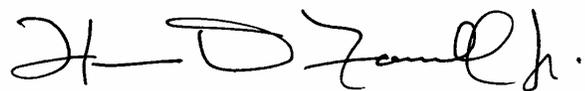
The Ways and Means Committee staff's assessments and projections presented in this report are reviewed by an independent panel of economists, including professionals from major financial corporations and prestigious universities, as well as respected private forecasters.

Assembly Speaker Sheldon Silver and I would like to express our appreciation to the members of this Board of Economic Advisors. Their dedication and expert judgment continue to be invaluable in helping to refine and improve our forecasts. While they have served to make the work of our staff the best in the State, they are not responsible for the numbers or views expressed in this document.

I wish to also acknowledge the dedicated and talented staff of the Assembly Ways and Means Committee and the many hours of work that went into producing this report. They play a vital role in our State's budget process.

As we continue our efforts toward enacting a timely budget that is fair and equitable for all New Yorkers, I look forward to working with each of you.

Sincerely,

A handwritten signature in black ink, appearing to read "H. D. Farrell, Jr.", written in a cursive style.

Herman D. Farrell, Jr.
Chairman

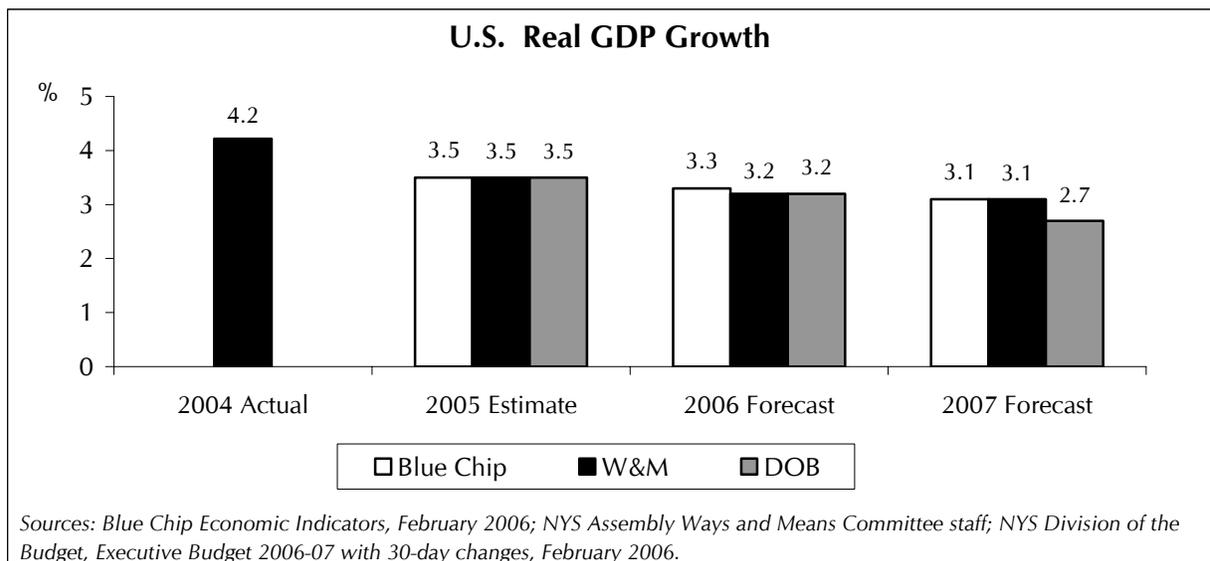
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EXECUTIVE SUMMARY

United States

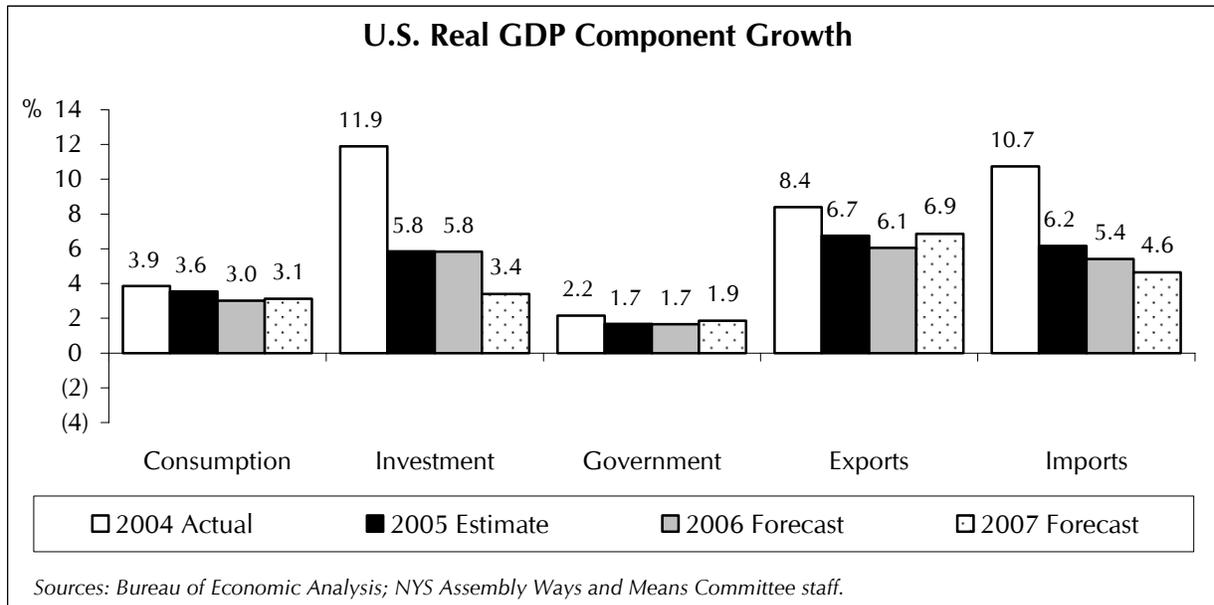
- Before hurricanes Katrina, Rita, and Wilma, the U.S. economy was steadily expanding at a rate near or above long-term trend growth. The national economy grew 4.1 percent during the third quarter of 2005 after growing 3.5 percent during the first half of 2005 and a healthy 4.2 percent year-over-year during 2004.
- In 2005, hurricanes had a severe regional impact. After Katrina, there was an immediate impact on the national economy through energy prices. Effects are also seen in inflation, and possibly weaker job and income growth. In the Gulf Coast region, which was hit by Katrina and Rita, all aspects of the economy have experienced devastation. Approximately 1.6 million workers were directly affected, and the region accounts for 1.1 percent of United States total nominal output. Nationally the greatest impact from the hurricanes has been seen in energy markets, where shortages and price increases have the potential to significantly slow economic growth.
- The national economy slowed significantly during the fourth quarter of 2005, growing a mere 1.1 percent from the third quarter. However, rebuilding activities in the Gulf Coast region will help boost economic growth in 2006.
- The national economy, as measured by real Gross Domestic Product (GDP), decelerated to 3.5 percent in 2005, after growing 4.2 percent in 2004.



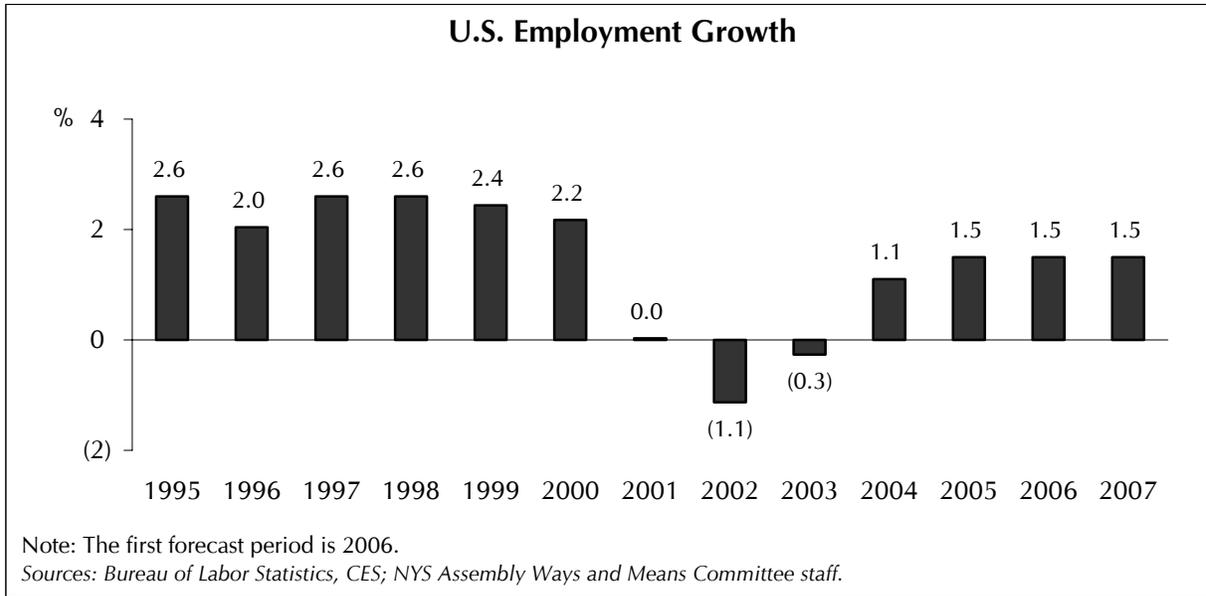
- Although a bit slower than during 2004, growth in personal consumption spending remained robust during most of 2005. It was fueled by a steady increase in the value of household assets (financial as well as non-financial), which was helped by long-term

interest rates that remained surprisingly low. Steady recovery in payroll employment and gains in real disposable personal income also helped support personal consumption spending growth.

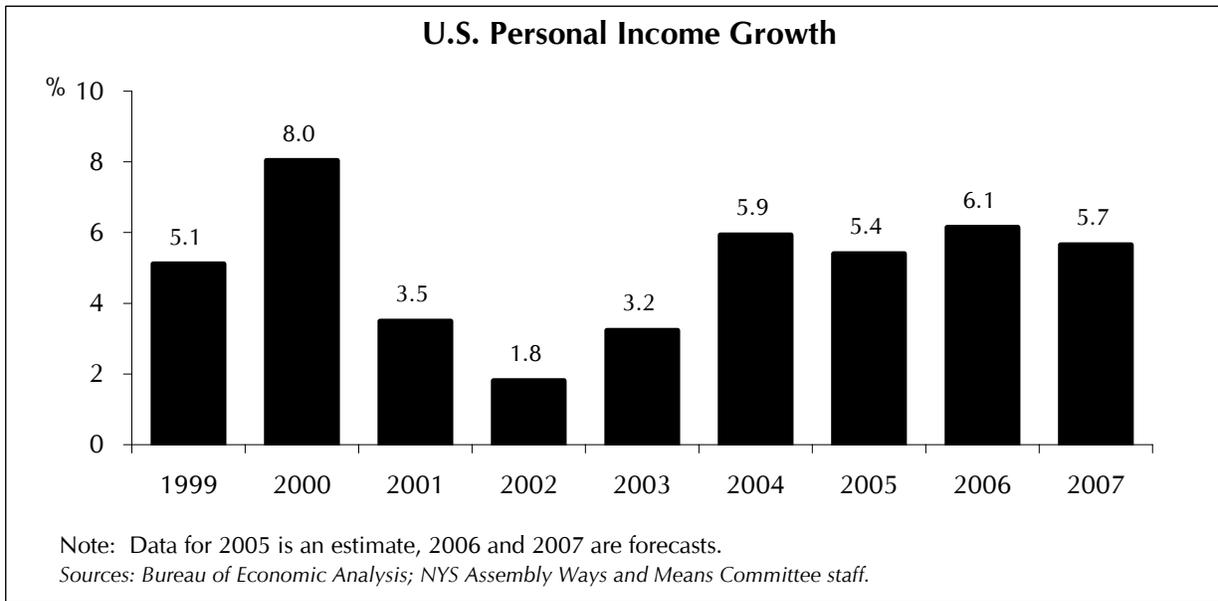
- The NYS Assembly Ways and Means Committee staff estimates that consumer spending will slow to 3.0 percent in 2006, due to consumers being more cautious of spending as well as growth in real disposable personal income being restrained by higher energy costs in the wake of hurricanes Katrina and Rita.



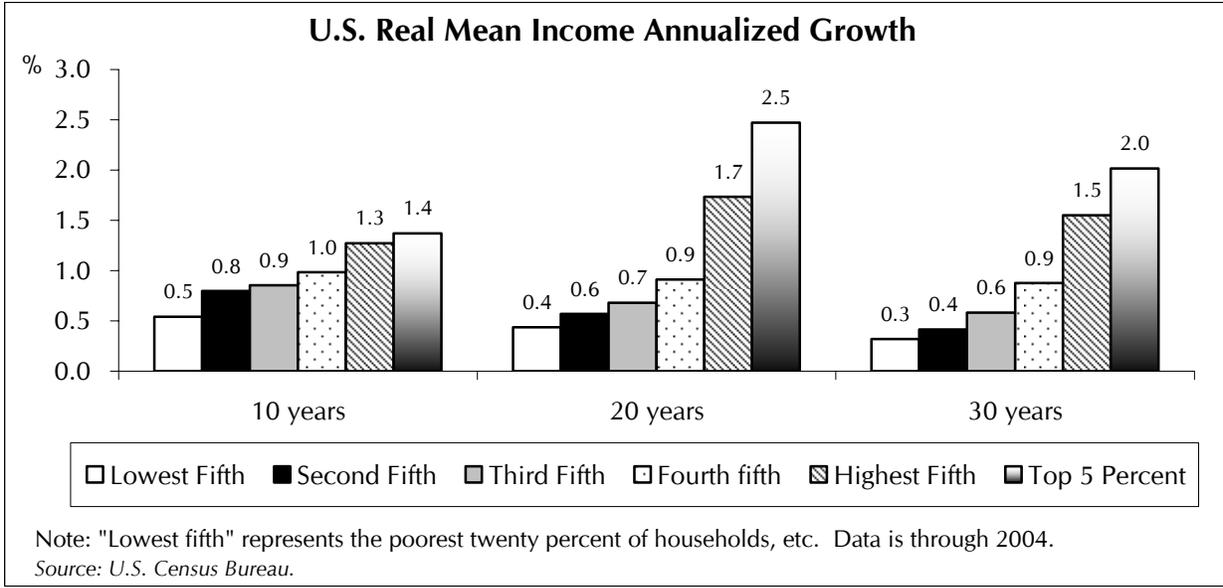
- Business capital spending will continue to be boosted by strong growth in corporate cash flow and favorable financing conditions, among other factors. Capital spending growth will remain steady in 2006 and then slow down to 3.4 percent in 2007 due mainly to weakness in residential construction activity.
- U.S. employment strengthened in 2004 and shows a profile of stable growth in 2005 and beyond. After growing 1.5 percent in 2005, payroll jobs are expected to grow another 1.5 percent in both 2006 and 2007.



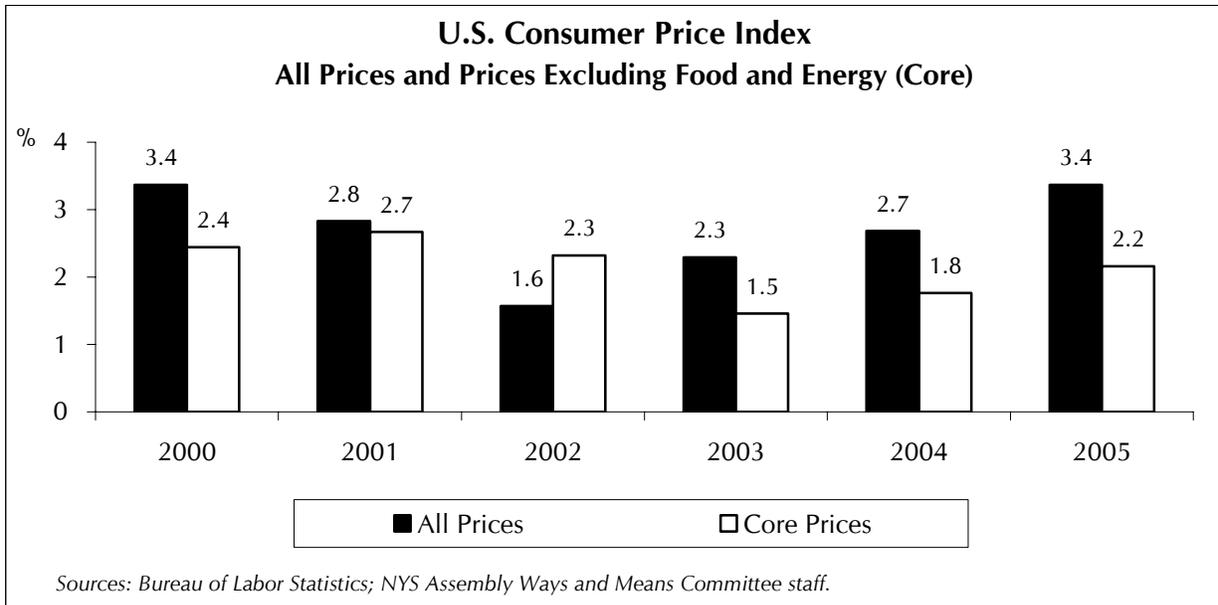
- The NYS Assembly Ways and Means Committee staff forecasts that most personal income components are expected to remain strong during the current forecast period. Personal income grew an estimated 5.4 percent in 2005 after an increase of 5.9 percent in 2004. It is forecast to further grow 6.1 percent in 2006 and 5.7 percent in 2007.



- Average incomes in the United States have been rising long-term. However, income inequality has been rising as well. Incomes have diverged, with poorer households experiencing less income growth across almost all time periods.

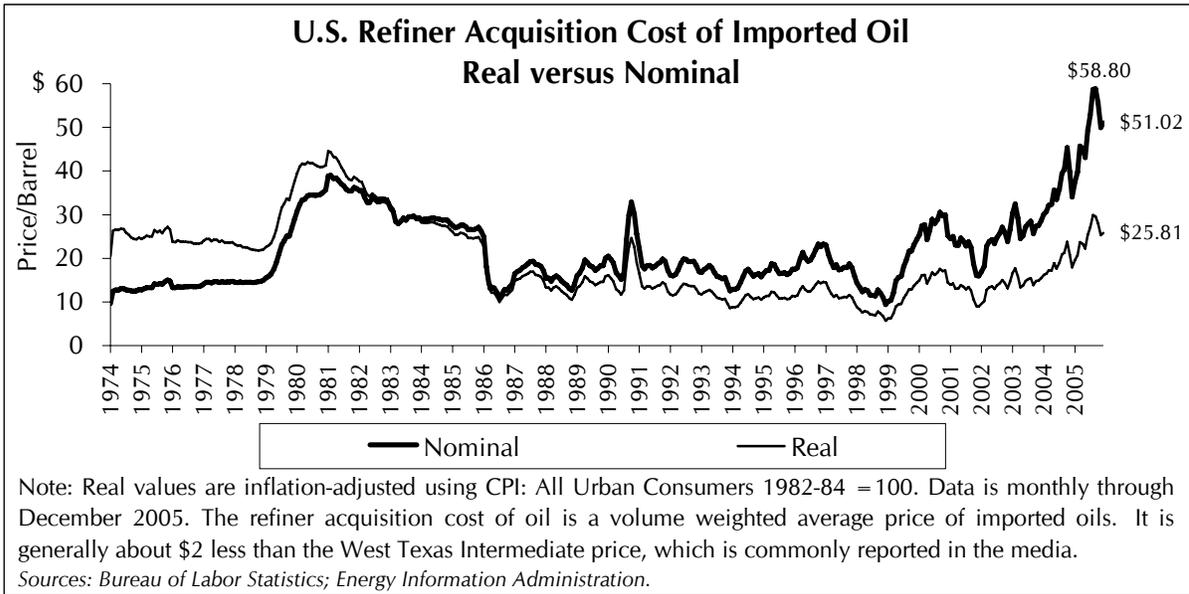


- The NYS Assembly Ways and Means Committee staff predicts that the general price level, as measured by the Consumer Price Index (CPI), will increase 3.2 percent year-over-year in 2006 and 2.7 percent in 2007. Prices increased 3.4 percent in 2005. The slowdown in CPI inflation in 2006 and 2007 is related to expected stabilization in oil prices as well as a slowdown in overall economic activity.



- Energy prices have followed a general upward trend for several years. This increase has been exacerbated in the past few years due to many factors, including: production constraints, dramatic growth in demand, weather-induced disasters, the War in Iraq, political and labor unrest in oil producing countries, uncertainty in the market, and

speculation on the part of investors. However, if the price of oil is adjusted for general price inflation, oil prices are not as high as in the early 1980s. To reach the inflation-adjusted record set in February of 1981 (monthly data), nominal prices now would have to reach almost \$89 per barrel. After Hurricane Katrina, gasoline prices approached the inflation-adjusted record set in the early 1980s but did not pass it.



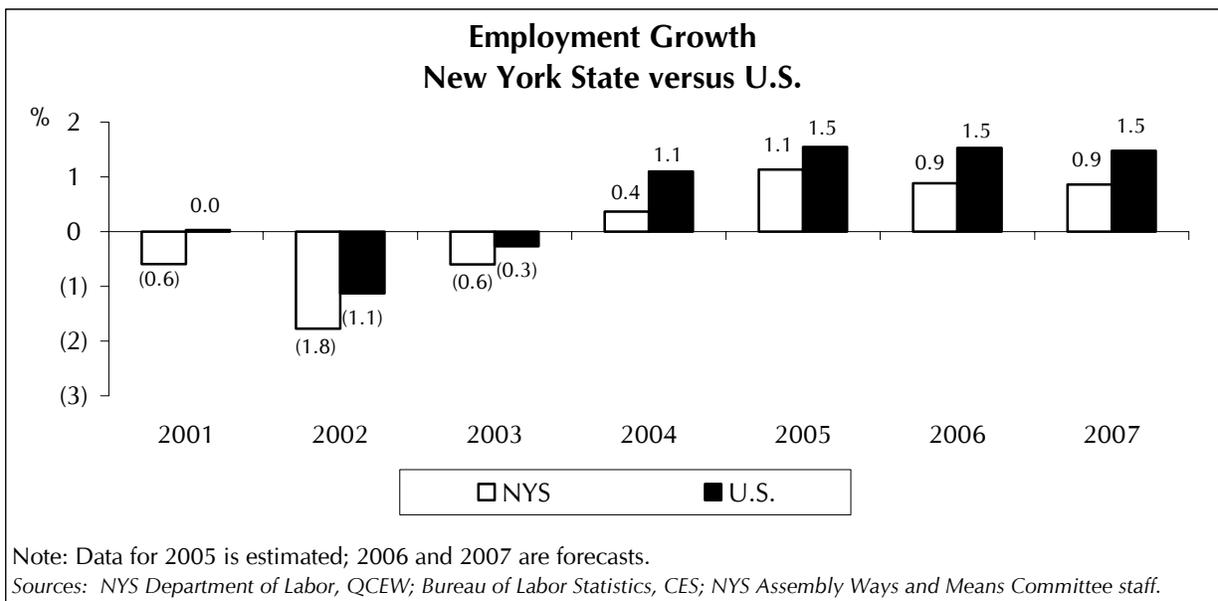
- The NYS Assembly Ways and Means Committee staff's overall national growth forecast for 2006 is 3.2 percent. It is the same as the Division of the Budget and 0.1 percentage point lower than Global Insight. It is 0.3 percentage point lower than both Moody's Economy.com and Macroeconomic Advisers.

U.S. Real GDP Forecast Comparison				
(Percent Change)				
	Actual	Estimate	Forecast	Forecast
	2004	2005	2006	2007
Ways and Means	4.2	3.5	3.2	3.1
Blue Chip Consensus	4.2	3.5	3.3	3.1
Division of the Budget	4.2	3.5	3.2	2.7
Moody's Economy.com	4.2	3.5	3.5	3.0
Macroeconomic Advisers	4.2	3.5	3.5	3.4
Global Insight	4.2	3.5	3.3	2.7

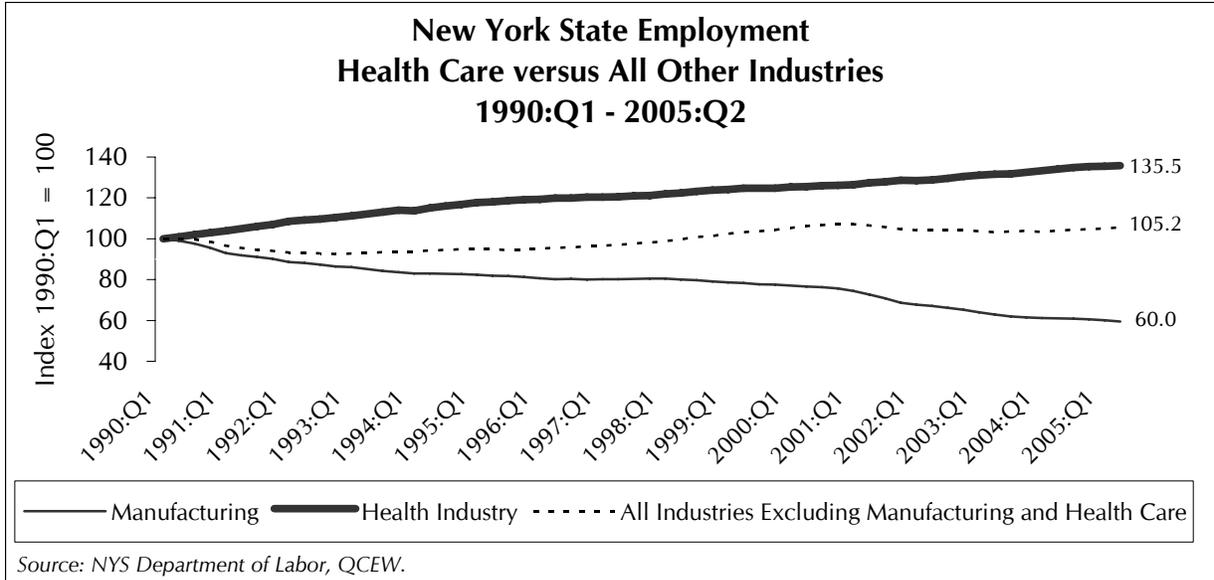
Sources: NYS Assembly Ways and Means Committee staff; Blue Chip, February 2006; NYS Division of the Budget, Executive Budget 2006-07 with 30-day changes, February 2006; Moody's Economy.com, February 2006; Global Insight, February 2006; Macroeconomic Advisers, January 2006.

New York State

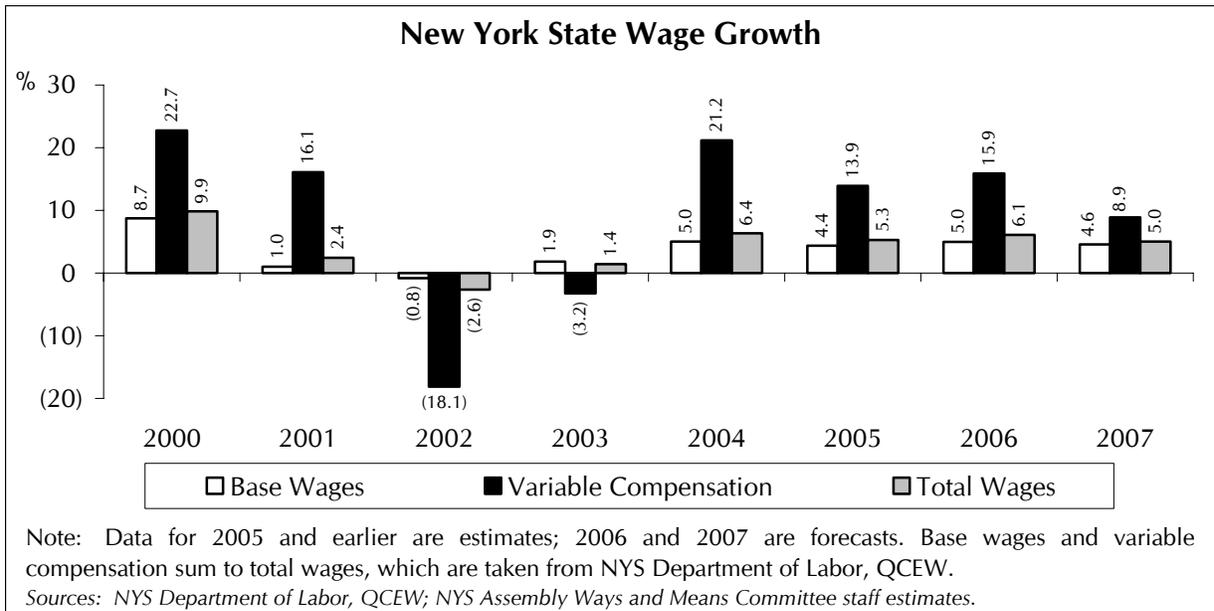
- The New York State economy lags the United States economy in terms of employment growth. However, the State will continue to benefit as the nation maintains an expansion.
- The percent gain in New York State employment from the State employment trough (2003:Q2) to the last forecast quarter (2008:Q1) is expected to be 4.1 percent, compared to 6.8 percent in the United States in the same period. If New York State were to gain jobs at the same rate as the U.S. during the period of employment expansion, the State would gain 225,400 additional jobs.



- The largest sectoral employment level gains in the State in 2006 are expected to be in education and health, retail trade, and professional services.
- Manufacturing job losses in 2006 and 2007 are expected to continue at rates similar to the rate of job loss in 2005.
- While most sectors lost jobs during the 2001 recession, the health industry continued to gain employment. In contrast to the manufacturing sector, the health industry is the only sector that showed significant gains during the 2001 recession.



- Employment growth for the securities industry turned positive in the first quarter of 2004 and is expected to remain strong for the entire forecast period. However, 2007 employment will still be only 94.9 percent of its 2001 peak.
- Wage growth in New York State has not again reached the high rates seen in 2000; however, wages are expected to show strong growth in 2006. The NYS Assembly Ways and Means Committee staff predicts that State total wages, which are the sum of base and variable wages, will grow 6.1 percent in 2006 and 5.0 in 2007.



- Variable compensation will grow faster than total wages over the forecast period and will make up 11.6 percent of total wages by 2007. Securities industry variable compensation is expected to grow faster than other industries in 2006 and in 2007.
- In 2005, New York State capital gains are estimated to have grown 32.3 percent. This will be followed by increases of 5.4 percent in 2006 and 15.8 percent in 2007.
- The NYS Assembly Ways and Means Committee staff's employment growth forecast for 2006 is 0.2 percentage point higher than the Division of the Budget forecast and 0.1 percentage point higher than Moody's Economy.com forecast. The 2007 forecast is 0.4 percentage point higher than Moody's Economy.com, and 0.2 percentage point higher than the Division of the Budget forecast.

NYS Forecast Comparison				
(Percent Change)				
	Actual	Estimate	Forecast	Forecast
	2004	2005	2006	2007
Employment				
Ways and Means	0.4	1.1	0.9	0.9
Division of the Budget	0.6	0.9	0.7	0.7
Moody's Economy.com	0.5	0.9	0.8	0.5
Wages				
Ways and Means	6.4	5.3	6.1	5.0
Division of the Budget	6.4	5.1	5.9	5.1
Moody's Economy.com	6.1	4.6	3.3	4.4

Sources: NYS Assembly Ways and Means Committee staff; NYS Division of the Budget, Executive Budget 2006-07 with 30-day changes, February 2006; Moody's Economy.com, February 2006.

- The NYS Assembly Ways and Means Committee staff's wage growth forecast for 2006 is 0.2 percentage point higher than the Division of the Budget's forecast, and 2.8 percentage points higher than Moody's Economy.com forecast. The 2007 forecast is 0.6 percentage point above Moody's Economy.com, and 0.1 percentage point lower than the Division of the Budget's forecast.

INTRODUCTION

United States Economy

Before Hurricane Katrina made its second landfall in the Gulf Coast region on August 29, 2005, the U.S. economy was steadily expanding at a rate near or above long-term trend growth. Widespread concern triggered by a series of weak data in the early spring of 2005 turned out to be overblown. Real GDP growth for the first quarter of 2005 was revised up from 3.1 percent in the “advance” estimate released in April to 3.5 percent in the “preliminary” estimate in May to 3.8 percent in the “final” estimate in June. The national economy grew 3.5 percent during the first half of 2005 after growing a healthy 4.2 percent year-over-year during 2004. Payroll employment growth, though still sluggish compared to earlier recoveries, was also steadily improving (see Figure 1).

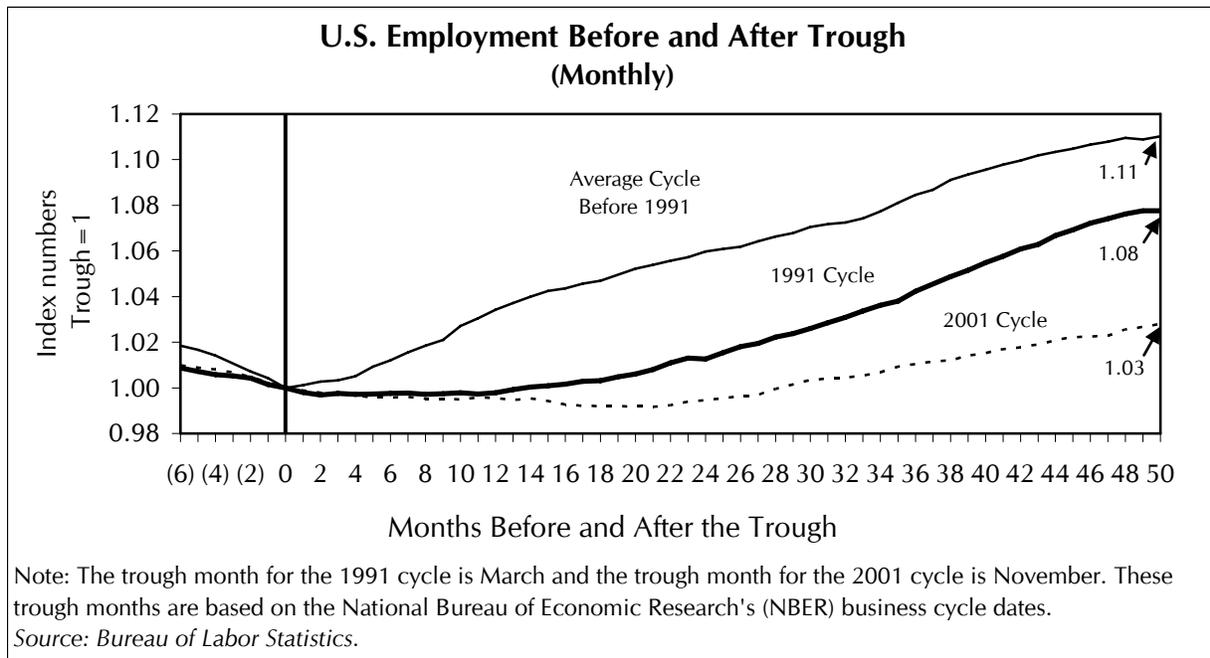


Figure 1

The near- or above-trend growth in national output that was underway before Hurricane Katrina was helped by upbeat consumption spending, strong residential construction activity, and robust business capital spending on equipment and software. Behind the spending of consumers and businesses were solid gains in real disposable personal income, steady appreciation in household equity as well as home prices, and sturdy growth in corporate profits.¹ Household assets in real estate grew 8.3 percent in

¹ In addition, fiscal as well as monetary stimuli has helped fuel spending by households and businesses since 2000. Although mounting federal budget deficits started restraining federal spending growth, federal as well as state and local governments are expected to inject over \$60 billion of aid money in the Gulf Coast region stricken by Hurricane Katrina.

2004 after growing some 10 percent each year since 1998. Household assets held in corporate equities and mutual fund shares grew 9.7 percent in 2004 after growing an impressive 55.4 percent in 2003, ending three consecutive years of double digit decline. Despite rising energy prices, disposable personal income, adjusted for price inflation in consumer goods in general, rose 2.2 percent on average over the past eight quarters. Corporate profits grew at a double digit rate for three years in a row, facilitating business capital spending.

The composite index of U.S. coincident indicators has risen every month (with the exception of three months) since April 2003, indicating the U.S. economy is still expanding (see Figure 2).² Although the index of U.S. leading economic indicators, a key gauge of future economic activity, recently declined for three months in a row, it was due mainly to weak consumer confidence and higher jobless claims, especially following hurricanes Katrina and Rita. The index rebounded in October 2005 and is still higher compared to the same period a year ago.³

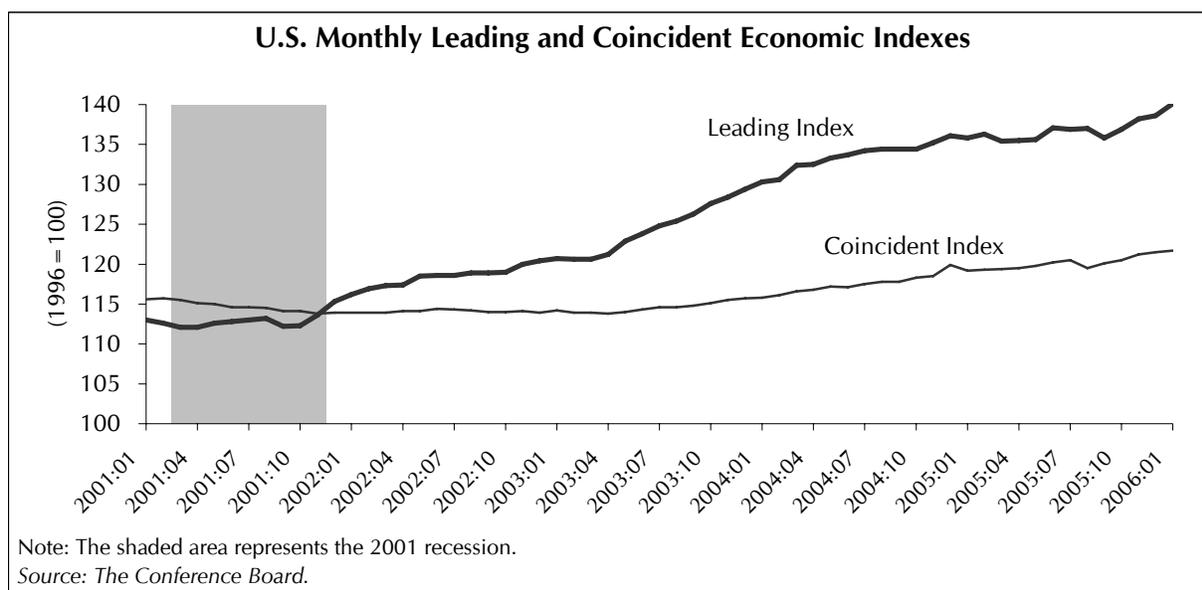


Figure 2

² The Conference Board’s composite index of U.S. coincident indicators consists of nonfarm payroll employment, real personal income less transfer payments, real sales in the manufacturing and trade sectors, and industrial production.

³ The Conference Board’s composite index of U.S. leading indicators consists of ten monthly time series. These include the average weekly hours worked by manufacturing workers, new orders for consumer goods, new orders for non-defense capital goods, stock prices measured by the S&P 500 composite stock price index, initial jobless claims, vendor performance, building permits, money supply measured by M2 adjusted for general price inflation, consumer expectations, and the spread between the 10-year Treasury note yield and the federal funds rate.

The economic disruption caused by hurricanes Katrina and Rita has been massive in the Gulf Coast region (see the Economic Impact of Hurricanes section on page 5). The national economy also slowed to a mere 1.1 percent growth during the fourth quarter of 2005. However, it did not bring about an economic downturn to the nation as a whole. With the total recovery cost estimated at some \$200 billion, rebuilding and recovery activities are expected to be substantial.

In the near future, personal consumption spending should be helped by steady growth in personal income, despite rising energy prices. Employment growth, though still sluggish compared to previous recoveries and likely to be weakened temporarily by disruptions in Gulf Coast states, is expected to recover throughout 2006 and continue thereafter.

Although there is a growing concern about the possibility of a bust in the housing market boom in the near future, continued growth in the housing market (both existing and new home sales have been at record highs) should help support household net worth growth at least in the next few quarters.⁴ Housing starts continued to show strength throughout most of 2005, defying economists' expectations. As more capacity is being utilized by business and industrial production is rising (see Figure 3), business capital spending will likely continue to expand.⁵ It also will be helped by the recent improvement in corporate balance sheets as well as the big surge in business cash flow seen over the past few years.

Although interest rates have started rising, business financing conditions are still quite favorable. Inventory investment rebounded significantly during 2004 and, despite a recent inventory correction in the automobile industry, should remain strong as the inventory-to-sales ratio is still quite low. Weakness in the domestic automobile industry will be a negative factor, but strength in other industries will compensate for this. Net exports will be less of a drag on economic growth as the U.S. dollar is expected to resume depreciation during 2006. Growth in federal as well as state and local government spending in efforts to rebuild the hurricane-stricken areas will also help support the economy during 2006.

⁴ See, for example, Mark Zandi, "Where are the Regulators?" *Dismal Scientist*, Moody's Economy.com, November 1, 2005, <http://www.economy.com/dismal/pro/article.asp?cid=18664&p=1>.

⁵ In September 2005 capacity utilization fell 1.2 percentage points and industrial production dropped 1.3 percent. This decline was caused mainly by hurricanes Katrina and Rita.

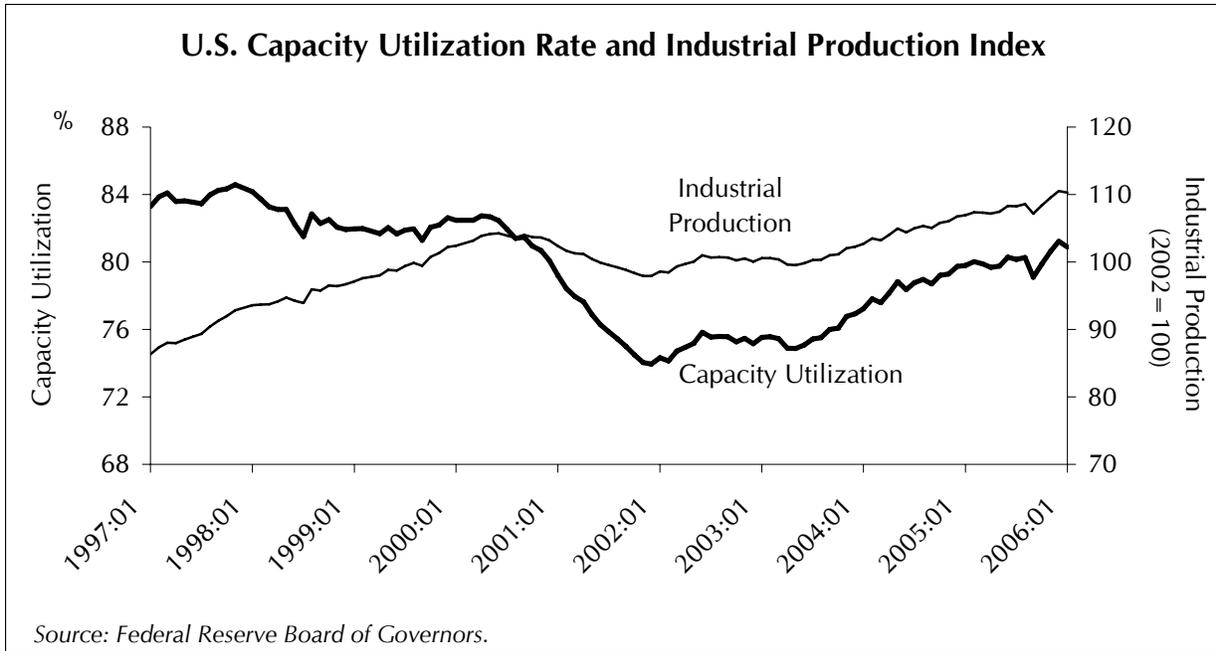


Figure 3

Oil prices are expected to stabilize in the coming months. Although oil prices (measured by the refiner’s acquisition cost) have been at a record high in current dollars, at the end of the third quarter of 2005 they were still just about half of the 1981 peak when adjusted for general price inflation (see the Prices section on page 37).

The core consumer price index, which excludes from the overall consumer price index more volatile items such as energy and food, increased 1.8 percent in 2004.⁶ It further increased 2.2 percent in 2005. This recent gain in core CPI was caused by underlying fundamentals that put upward pressure on the general price level. Productivity growth decelerated to 2.6 percent in the first half of 2005 after growing 3.8 percent in 2003 and 3.4 percent in 2004. At the same time, unit labor costs for the U.S. non-farm business sector rose 3.5 percent in the first half of 2005, a substantial acceleration from the 0.2 percent increase in 2003 and the 1.1 percent increase in 2004.⁷ As high energy prices

⁶ The core price index excludes volatile food and energy prices from the calculation of the price index. Changes in food and energy prices are often temporary, and have the potential to rapidly reverse. Many times, these spikes are due to supply shocks which do not respond to changes in monetary policy. Therefore, movement in the core price index may more closely reflect changes that the Federal Reserve has control over. See also, John Silvia, Mark Vitner, and Jason Schenker, *What’s Ahead For Inflation?* (Wachovia Economics Economic Commentary, November 23, 2005).

⁷ The recent labor cost surge represented by unit labor costs or compensation per hour may have exaggerated the movement of true labor costs. That is because, unlike unit labor costs, the employment cost index for U.S. private sector compensation advanced only 2.7 percent in the first half of 2005, decelerating from the 4.0 percent growth for both 2003 and 2004. This disparity between two measures of labor costs was due in large part to the fact that compensation per hour includes items that employment cost index does not, notably stock options and other bonuses that surged in the first quarter of 2005. Employment cost index does not include the compensation of self-incorporated professional workers (e.g. doctors and lawyers) and the self-

have persisted longer than expected since 2003, companies have been more and more stressed to pass part of the increased costs on to consumers. In addition to the damage to the U.S. energy infrastructure caused by the 2005 hurricanes, these fundamental forces will likely put further upward pressure on core CPI. Overall CPI inflation accelerated in the second half of 2005, resulting in estimated inflation of 3.4 percent for the whole year, following the 2.7 percent seen during 2004. With the energy market expected to stabilize in the course of 2006, however, overall price inflation will likely slow to 3.2 percent during 2006.

While productivity growth is expected to slow to a more sustainable rate of around 2.5 percent, the nation will likely gain around 166,700 payroll jobs a month during 2006. The employment recovery will be broad, cutting across economic sectors, with services leading the way.

Stock prices using the S&P 500 index grew modestly in 2005, increasing 6.8 percent using yearly average values. Healthy corporate profits and dividend income will support further improvement in the corporate equity market in 2006, although rising interest rates may rein in equity year-end valuation.

Despite the positive signs mentioned above, the economic environment remains uncertain, with many risks to the current forecast. The future course of oil prices is certainly a major risk factor. It is also uncertain how long consumption can remain strong as interest rates are expected to rise and the housing market may cool. Large deficits in the U.S. current account and federal budget may have very serious economic repercussions both at home and abroad. Any future terrorist attack as well as further deterioration of the situation in Iraq can have a large impact on spending and investment, as well as hinder confidence in the future performance of the economy. Major job cuts in the domestic automobile industry are also a threat to the economy, particularly if this trend spreads to other industries with high pension and health care costs relative to foreign competitors.

Economic Impact of Hurricanes

Several hurricanes made landfall on United States soil in 2005. On August 29, Hurricane Katrina made its second landfall in the United States Gulf Coast region. The storm had a devastating effect on the area, both human and economic. The death toll was more than 1,000 persons. Following Katrina, on September 24, Hurricane Rita made its landfall in Texas near the Louisiana border. The storm was the strongest ever recorded in the Gulf of Mexico. Areas of Texas were heavily damaged and sections of New Orleans were once again under water. On October 24, Hurricane Wilma hit Florida after making

employed. Nor does it include the compensation of high-level corporate employees such as CEOs and other senior management. See Global Insight, *U.S. Executive Summary*, August 2005, 4-5.

landfall in Mexico. Wilma initially knocked out power to over 3.6 million people in Florida.⁸

All aspects of the local economies affected during the 2005 hurricane season have experienced devastation. Large hurricanes in the Gulf Coast region impact not only the regional economy of the affected areas, but also can hurt the national economy through energy prices and effects on inflation, and possibly weaker job and income growth. Hurricane Katrina affected approximately 1.6 million workers. The area also accounts for 1.1 percent of United States total nominal output.⁹

Nationally, the greatest impact during the 2005 hurricane season was seen in energy markets, where shortages and price increases have the real potential to significantly slow economic growth. The Gulf Coast is home to 47.4 percent of the United States refining capacity, and accounts for 28.7 percent of the nation's domestic oil production and one-fifth of its natural gas output.¹⁰ This area remains vulnerable to hurricanes in the future.

As of February 7, 2006, 225,000 barrels per day of oil production in the Gulf was closed temporarily (shut-in). Natural gas production shut-in was 400 million cubic feet per day. Only one refinery remained closed, although many were still operating below normal capacity.¹¹ The effects of the damage from Katrina were immediately felt in the gasoline market throughout the United States. Prices approached and came close to surpassing the record inflation adjusted levels that the country experienced in the 1980s.

Shipping and trade are affected by hurricanes, as the Gulf Coast is also home to several seaports which together account for almost one-fifth of the nation's shipping of goods, both exports and imports. In particular, the New Orleans port is one of the nation's deepest, making it difficult for large vessels to go elsewhere.

The estimates of insured losses range widely. Insured losses from Wilma could be \$5 billion to \$9 billion.¹² Estimates of Katrina damage are between \$14 billion to \$60 billion. Rita damage estimates are between \$2.5 billion to \$6.6 billion. The combined losses from Katrina and Rita are on a similar magnitude with the September 11th attacks and

⁸ U.S. Department of Energy, *Office of Electricity Delivery and Energy Reliability*, "Gulf Coast Hurricane Situation Report," <http://www.electricity.doe.gov> (October 14, 2005).

⁹ Mark Zandi, "Katrina: The Economic Fallout," *Dismal Scientist*, Moody's Economy.com, August 30, 2005; Daniel Jester, "Katrina: Implications for the Fed," *Dismal Scientist*, Moody's Economy.com, August 31, 2005.

¹⁰ Energy Information Administration, "Daily Report on Hurricane Impacts on U.S. Energy," http://tonto.eia.doe.gov/oog/special/eia1_katrina.html (October 28, 2005).

¹¹ Energy Information Administration, Short-term Energy Outlook, <http://www.eia.doe.gov/emeu/steo/pub/contents.html> (February 7, 2006).

¹² "Wilma Among Top Three Most Costly Storms," *CNN Money*, <http://money.cnn.com/2005/10/24/news/economy/wilma/index.htm> (October 24, 2005).

Hurricane Andrew.¹³ It is likely that a large part of the population is permanently displaced from the area.

New York State Economy

New York State outperformed the nation in terms of wage growth in 2004. As Figure 4 shows, 2004 wages increased by 6.4 percent in the New York State, while in the nation, the increase was only 5.4 percent. This was strong growth. Employment rose in both the nation and the State; however the nation had a larger increase.

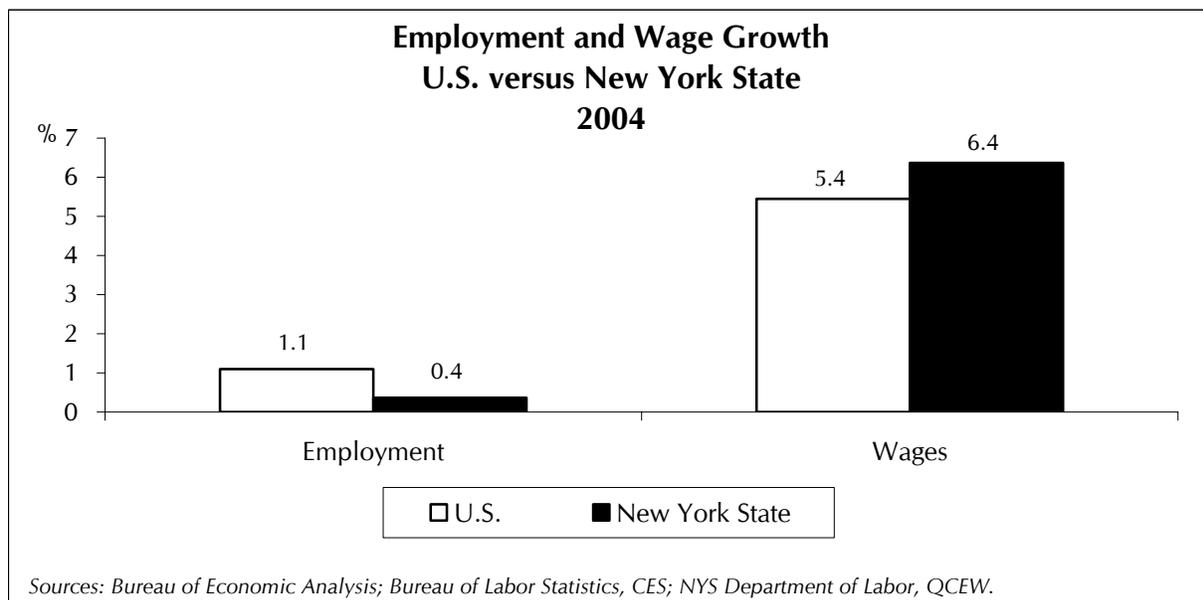


Figure 4

New York will continue to benefit as the rest of the nation continues to recover. New York City will help to fuel State growth, as New York City employment growth became positive in early 2004 and continues to post gains. However, the recovery of jobs from the 2001 recession has taken longer in the State than in the nation. The NYS Assembly Ways and Means Committee staff estimates that employment will grow slower than the nation throughout the forecast period.

New York State will be helped by strong growth from variable compensation, especially in the securities industry. The State's concentration in the industry often leads to a positive impact on State wage growth. The securities industry is the largest contributor to variable wages, and the outlook for this sector is currently positive. However, the inherent volatility in this industry presents a risk to the forecast.

¹³ CNN Money, "Insured Losses from Rita Seen Up to \$6B," September 24, 2005.

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UNITED STATES FORECAST

Gross Domestic Product

The NYS Assembly Ways and Means Committee staff estimates that the national economy, as measured by real Gross Domestic Product (GDP) growth, decelerated to 3.5 percent in 2005, after growing 4.2 percent in 2004 (see Figure 5). The deceleration in 2005 was a result of a decline in business capital spending growth as well as personal consumption spending growth. The economy had solid growth in the first three quarters of 2005, which helped it withstand adverse impacts from the hurricanes.

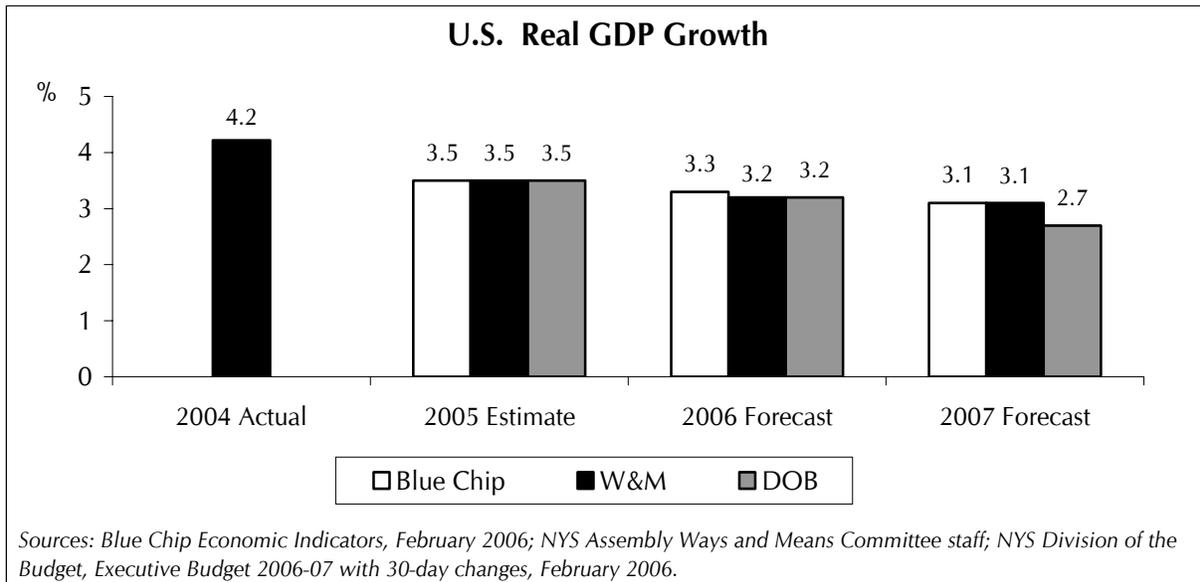


Figure 5

As personal consumption spending growth is expected to slow in 2006, real GDP growth is forecast to further decelerate to 3.2 percent year-over-year in 2006 (see Figure 6). Real GDP is forecast to grow 3.1 percent in 2007, a rate slightly lower than the long-term trend.

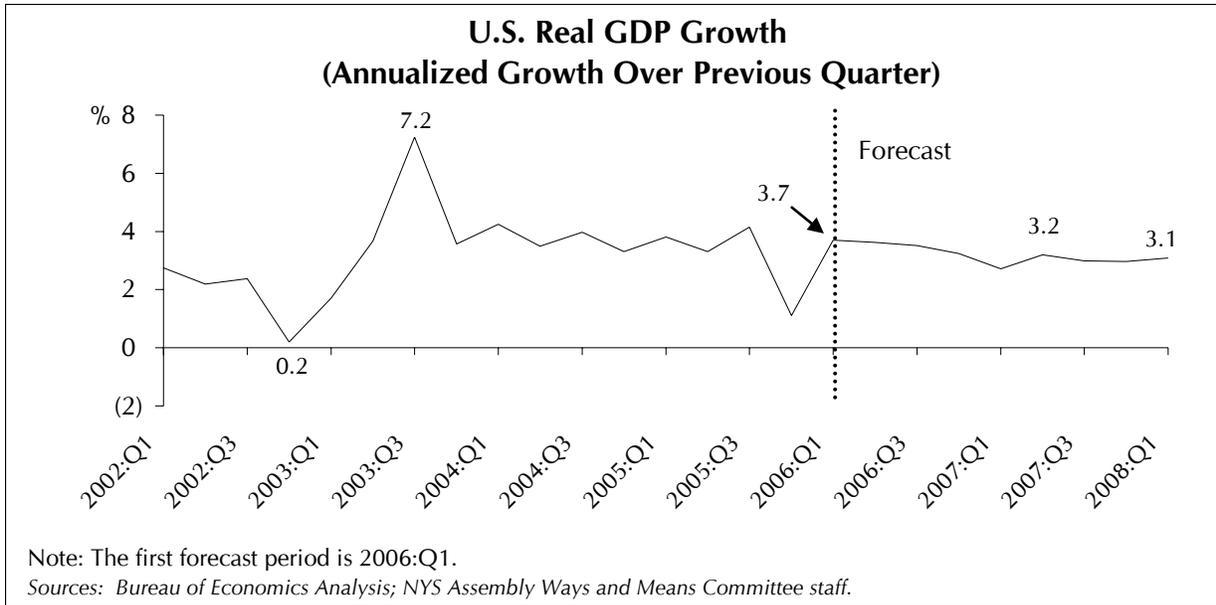


Figure 6

Consumption

Despite a significant increase in crude oil prices that cut into the consumer's purchasing power, personal consumption spending, adjusted for overall price inflation for consumer goods, grew a brisk 3.9 percent year-over-year during 2004. Except for the second quarter of 2004 when overall consumer spending growth dropped to a mere 1.9 percent, it grew at an annual rate of 4.3 percent to 4.7 percent each quarter during 2004.

This healthy growth in personal consumption spending was fueled by a steady increase in the value of household assets (financial and non-financial), which was helped by long-term interest rates that remained surprisingly low as well as federal tax refunds. Steady recovery in payroll employment and gains in real disposable personal income also helped support personal consumption spending growth. During 2005, personal consumption spending grew an estimated 3.6 percent.

Sharply rising energy prices since late 2003 have raised the price index for overall personal consumption expenditures and reduced real disposable personal income growth. Economic disruptions caused by the hurricanes and resulting higher energy prices have restrained real personal income growth. As a result, consumer spending growth is estimated to have slowed to a mere 1.1 percent in the fourth quarter of 2005. But with insurance benefits as well as government aid money expected to flow into the disaster-stricken region sooner rather than later under mounting political pressure, consumer spending will likely grow at a rate above long-term trend growth during the first half of 2006. Energy prices, which have spiked since Hurricane Katrina made landfall in August 2005, are expected to stabilize (see Oil and Energy Prices on page 39). As payroll

employment is also expected to gradually recover throughout 2006 from the disruptions, personal income growth will likely continue to be robust after showing temporary weakness in the third quarter of 2005 (see Figure 7).

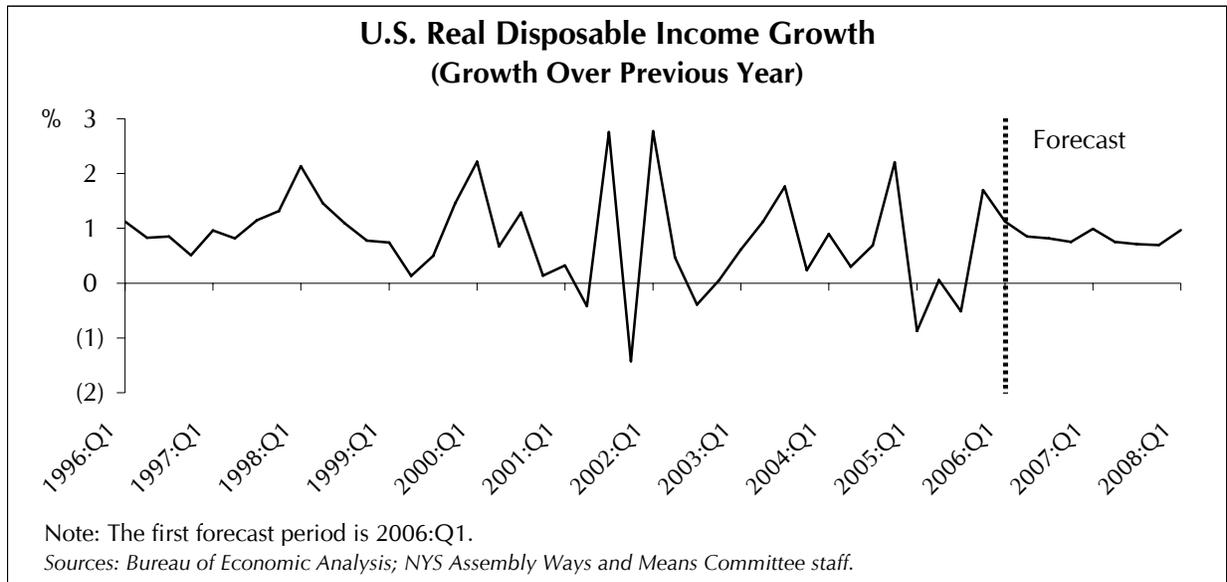


Figure 7

Household net worth continued to grow during 2004, thanks to steady growth in real estate values and continued recovery in corporate equity values (see Figure 8). Corporate equity markets have remained calm even after the recent natural disaster and will likely improve further in coming months as economic expansion continues. The housing market has remained strong—both existing and new home sales have been at record highs. Although it is assumed that household net worth will continue to grow during the current forecast period, helping to support consumption spending growth, there is a growing concern about the housing market possibly cooling down in the near future (see Housing Market section on page 21).

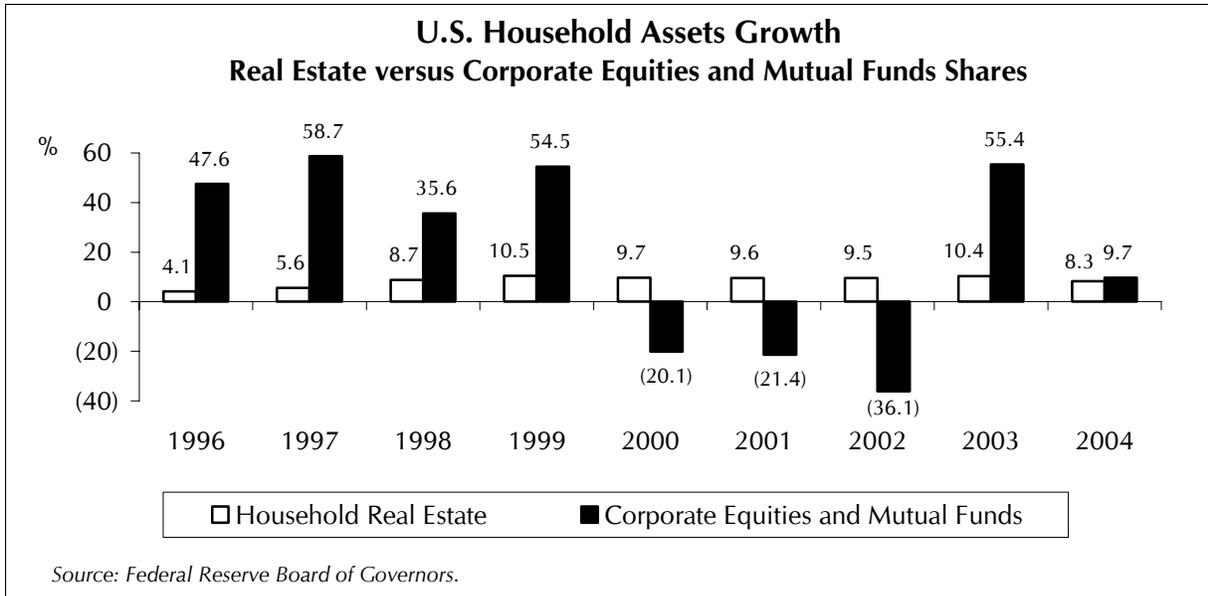


Figure 8

New orders for consumer goods continue to exhibit a steady upward trend, signaling that consumer spending growth will continue in the coming months (see Figure 9).



Figure 9

There are, however, forces that may negatively affect consumer spending. Although personal income shot up sharply due to the Microsoft dividend of \$32.4 billion paid out on December 2, 2004, the record low personal savings rates seen in the most recent seven

months may force consumers to be more cautious of spending and increase saving (see Figure 10).¹⁴ With short-term and long-term interest rates expected to rise, cash flow from refinancing may drop, further restraining consumer spending.

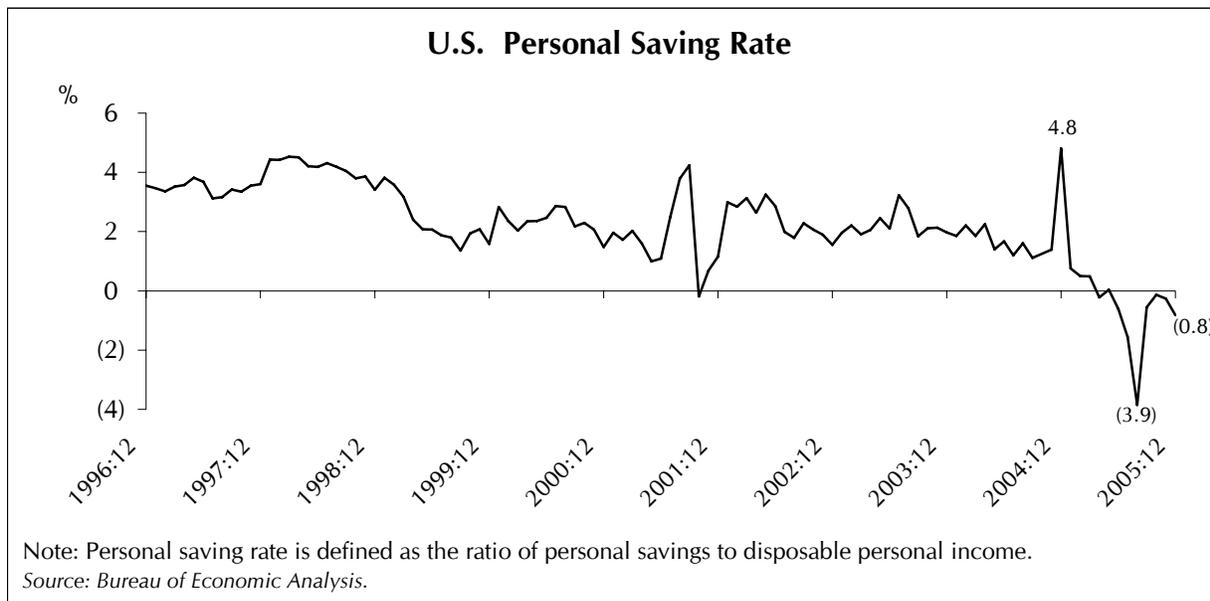


Figure 10

Much of the growth in the total compensation (i.e., wages and salaries plus benefits) of workers has been attributed to faster growth in various benefit payments since 2000 (see Figure 11).¹⁵ The benefits portion of total compensation has increased on average 5.5 percent year-over-year since 2000, whereas total compensation has increased 3.8 percent. This means that take-home pay has not been rising as much. As a result, consumers can get squeezed easily if cash flow from alternative sources such as cash-out refinancing decreases as interest rates rise. Employment growth is also uncertain, posing a major downside risk to consumer income.

¹⁴ The recent negative savings rates seen for seven consecutive months starting June 2005 are unprecedented in terms of both duration and magnitude. Since 1929 the only other times when the U.S. annual personal savings rate was negative were 1932 (-0.9 percent) and 1933 (-1.5 percent). Since the personal savings rate is defined as the percentage of after-tax personal income that is unspent during each time period, a negative savings rate means that consumers spend more than what they earn after paying taxes; the shortfall in after-tax earnings relative to spending should be made up for by income other than personal income, such as capital gains or non-income cash flow such as cash-outs from mortgage refinancing. When adverse shocks to the economy are believed to last only temporarily, consumers tend to maintain their normal spending pattern by saving less or borrowing more. When adverse shocks to the economy are believed to last longer than temporarily, however, consumers may give up their normal spending pattern and reduce spending.

¹⁵ Benefits include: paid leave; supplemental pay such as overtime; life, health, and disability insurance; retirement savings; legally required benefits such as social security and unemployment insurance; and other benefits such as severance pay. Benefits account for about 28 percent of total compensation.

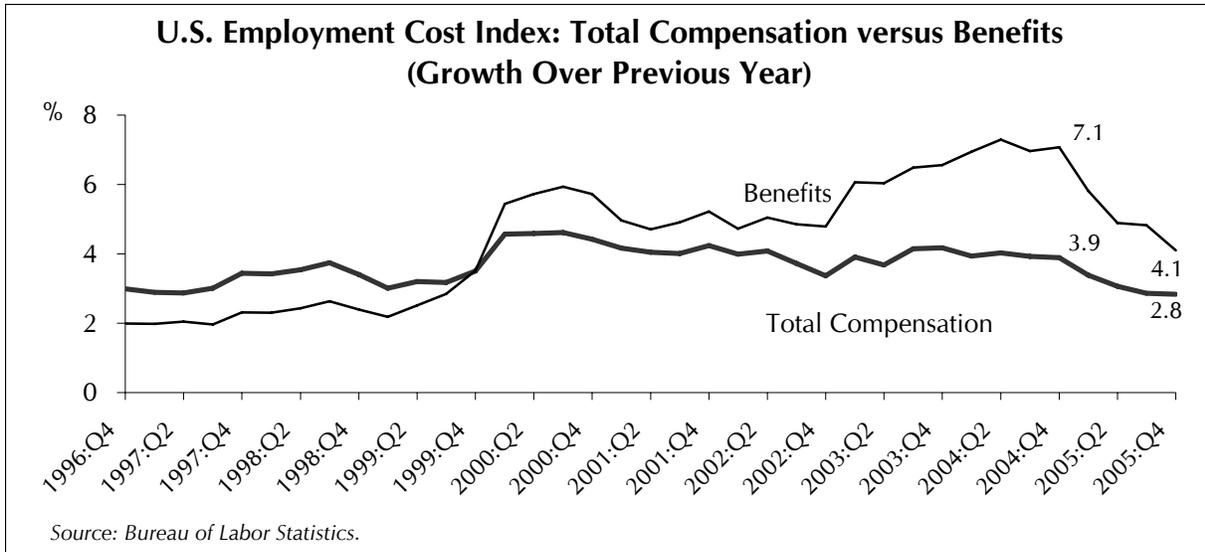


Figure 11

The Assembly Ways and Means Committee staff estimates that consumer spending, after adjusting for price inflation, increased 3.6 percent during 2005 after growing 3.9 percent during 2004. It will then slow to 3.0 percent in 2006, caused by restrained growth in real disposable personal income due to higher energy costs in the wake of hurricanes Katrina and Rita. As energy prices, among other factors, are expected to stabilize with improvement in energy markets, consumer spending will continue to grow by 3.1 percent in 2007 (see Figure 12 and Table 1).

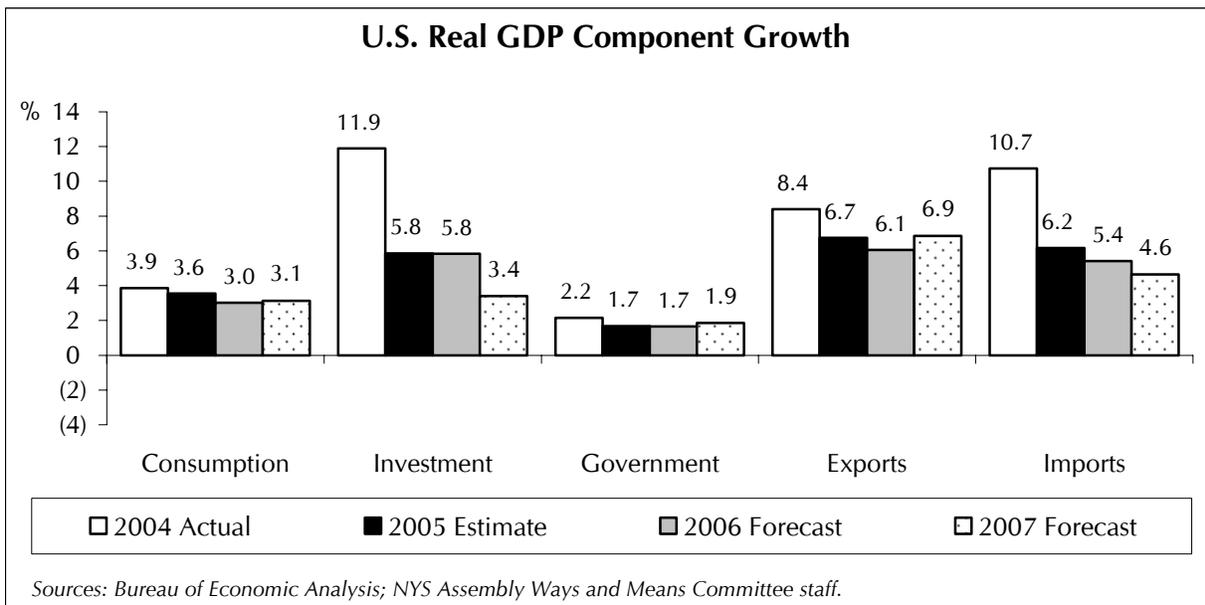


Figure 12

Table 1

U.S. Economic Outlook				
(Percent Change)				
	Actual	Estimate	Forecast	Forecast
	2004	2005	2006	2007
Real GDP	4.2	3.5	3.2	3.1
Real Consumption	3.9	3.6	3.0	3.1
Real Investment	11.9	5.8	5.8	3.4
Real Exports	8.4	6.7	6.1	6.9
Real Imports	10.7	6.2	5.4	4.6
Real Government	2.2	1.7	1.7	1.9
<i>Federal</i>	5.2	2.0	1.4	1.1
<i>State and Local</i>	0.4	1.5	1.8	2.3
Personal Income	5.9	5.4	6.1	5.7
Wages & Salaries	5.4	6.0	5.4	5.3
Transfer Income	6.2	6.9	6.7	7.4
Corporate Profits (Accounting Basis)	13.0	34.6	7.2	5.5
Corporate Profits (Economic Basis)	12.6	15.9	9.1	5.8
Productivity	3.4	2.6	2.5	2.4
Employment	1.1	1.5	1.5	1.5
CPI-Urban	2.7	3.4	3.2	2.7
S&P 500 Stock Price	17.3	6.8	9.0	7.7
Treasury Bill Rate (3-month)*	1.4	3.2	4.6	4.7
Treasury Bond Rate (10-year)*	4.3	4.3	5.0	5.3

* Annual average rate.
Sources: Bureau of Economic Analysis; Bureau of Labor Statistics; Federal Reserve Board of Governors; Standard & Poor's; NYS Assembly Ways and Means Committee staff.

Services consumption, the least volatile as well as the largest component of consumption (about 57 percent of the total), grew 3.0 percent during 2004 following 2.0 percent growth during 2003.¹⁶ Growth is estimated to have slowed slightly to 2.9 percent during 2005, due in part to slower growth in real disposable personal income caused by higher energy prices. Growth in consumer spending on services is forecast to rebound gradually during 2006 and 2007 due to robust growth in consumer spending on medical care and “other” services including personal business services.

Nondurable goods consumption grew 4.7 percent year-over-year during 2004, accelerating further from the 3.2 percent growth in 2003. Energy consumption, which accounts for some 10 percent of total nondurable goods consumption, has surged in nominal terms and will likely remain high due to higher energy prices. Energy consumption spending adjusted for increases in prices, however, actually declined 4.2 to 4.7 percent in the second and third quarters of 2005. As general price inflation accelerated to 3.4 percent in 2005 from 2.7 percent in 2004, consumers’ purchasing power in real

¹⁶ The 57 percent share is an average based on the last five years of data.

terms grew more slowly during 2005 over 2004, spoiling consumption spending on other nondurable goods. As a result, growth in total consumer spending on nondurable goods is estimated to have slowed to 4.4 percent year-over-year during 2005. It will further slow to 3.4 percent in 2006 and 2.6 percent in 2007.

Durable goods consumption, the most volatile as well as smallest component (about 13 percent of the total consumption), grew 6.6 percent year-over-year during 2003, after growing 4.3 percent or higher for several years in a row (see Figure 13). A good part of the steady growth in durable goods consumption for the past few years can be ascribed to the unusually strong auto sales due to various incentives. Auto sales and housing activity (which indirectly affects durable goods purchases) are not expected to achieve their current record levels in 2006.

Domestic automobile sales in particular present a cause for concern. Although total automobile sales from all sources remain strong, domestic automobile producers are declining in market share. General Motors has decreased its U.S. market share of units sold from 33.7 percent in 1993 to 27.5 percent in 2004, while Ford's share has declined from 25.8 percent to 19.1 percent over the same period. Partially as a result of this decline in share, General Motors has lost nearly \$4 billion in the first three quarters of 2005. The company maintains that it cannot stay competitive in the world market given current pension and health care costs. General Motors has 2.5 retirees for every active worker.¹⁷

On November 21, 2005, General Motors announced it was eliminating 25,000 jobs in addition to 5,000 jobs the company announced it was eliminating earlier in the year. Together, this represents a 17 percent cut in the company's North American workforce. Ford Motor Company announced on January 23, 2006, that it was cutting 25,000 to 30,000 jobs by 2012 and closing 14 facilities. The job cut represents 20 to 25 percent of Ford's North American workforce.¹⁸ The job cuts are from the second restructuring for Ford in four years. Ford previously closed five plants and cut 35,000 jobs, but its North American operations failed to improve. These job cuts will have significant ripple effects on the United States economy, reducing consumption. The cuts may also have a large negative impact on the Western New York region. It may also represent a larger problem for old, large United States corporations, particularly in the manufacturing sector. Legacy health care and pension costs have the potential to damage the competitive position of many more domestic companies.

Growth in consumer spending on durable goods is forecast to slow to 1.6 percent year-over-year during 2006, following an estimated 4.4 percent growth during 2005.

¹⁷ Dee-Ann Durbin, "General Motors to Cut 30,000 Manufacturing Jobs, Close Plants," *Associated Press*, November 22, 2005.

¹⁸ Dee-Ann Durbin, "Ford Slashing Up to 30,000 Jobs by 2012," *Associated Press*, January 23, 2006.

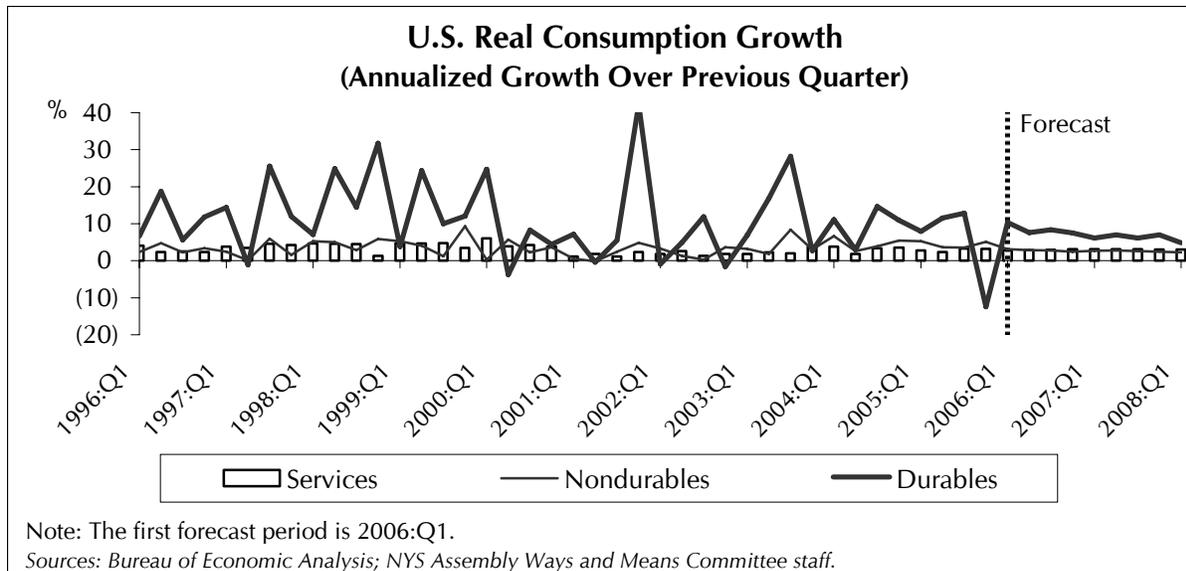


Figure 13

Investment

Private investment spending dropped sharply in the 2001 recession after an excessive run-up during the investment boom of the 1990s. It declined nearly 7.9 percent year-over-year during 2001 and another 2.6 percent in 2002. This created pent-up demand for business equipment and software, which, combined with capital depreciation tax incentives provided by the federal government, led to its strong rebound in 2003 and 2004. In particular, business spending on information-processing equipment and software increased 5.1 percent in 2003 and a strong 13.6 percent in 2004. On the other hand, business construction spending, which was hit particularly hard during the 2001 recession, declined 2.3 percent in 2001 and 17.1 percent in 2002. It continued to contract in 2003, declining 4.2 percent year-over-year. Business construction spending finally turned around during 2004, growing 2.2 percent year-over-year. In contrast, residential construction spending posted positive, though small, gains even during 2001 and 2002 due mainly to record low interest rates. Residential construction spending grew 0.4 percent in 2001, followed by a healthy 4.8 percent in 2002. It further accelerated to 8.4 percent year-over-year during 2003 and 10.3 percent during 2004.

Private investment spending continued to expand during 2005, growing 5.8 percent year-over-year after increasing an estimated 11.9 percent in 2004 and 3.9 percent in 2003. As overall economic activity is expected to continue to expand, private investment spending is also forecast to grow 5.8 percent in 2006. It will then slow to 3.4 percent in 2007 due mainly to weakness in residential construction activity.¹⁹

¹⁹ Although residential construction activity will pick up due to rebuilding activities in the Gulf Coast region, rising interest rates as well as rising construction materials prices will likely more than offset the post-Katrina boost. Overall residential construction spending will weaken in 2006, compared to 2005.

Several other factors also will contribute to furthering gains in business investment spending including:

- * **Strong growth in corporate cash flow** (see the Corporate Profits section on page 43). Corporate profits have been steadily improving since the end of 2001.
- * **Still favorable financing conditions** helping to keep borrowing costs down for investment spending (see the Interest Rates section on page 46). The result is affordable borrowing for needed capital expenditures.
- * **Nonmilitary capital goods orders** rising in recent months (see Figure 14).²⁰ As businesses continue to see signs of an economic expansion, orders for capital equipment should continue to increase.
- * Both **capacity utilization and industrial production** on the rise supporting further expansion in business capital spending (see Figure 3 on page 4).

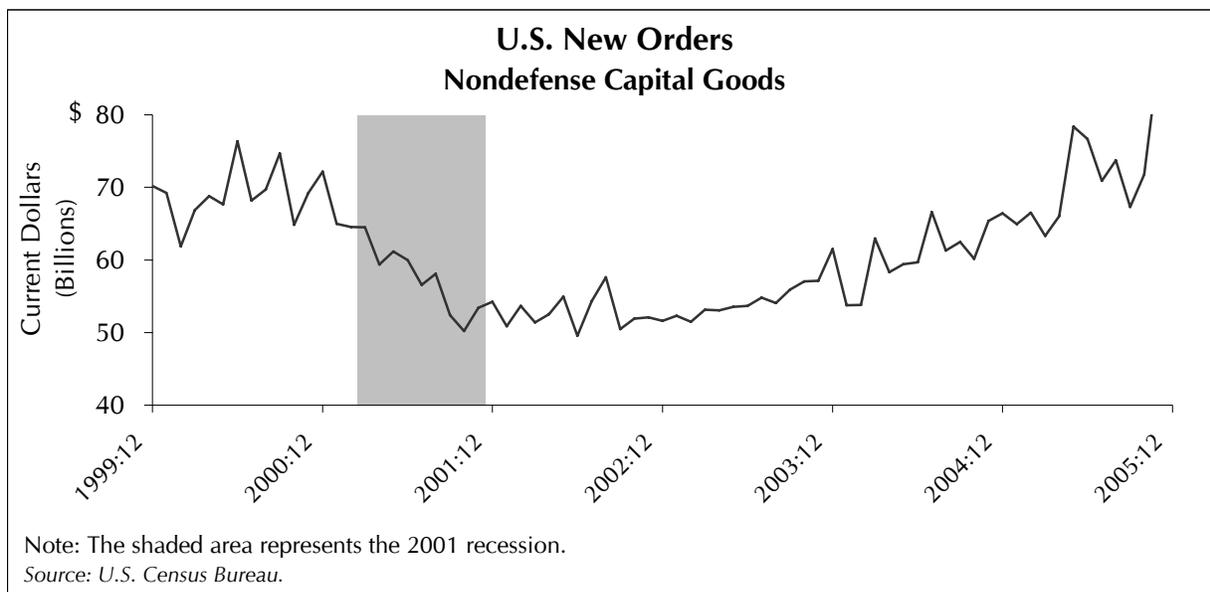


Figure 14

In constant dollar terms, business spending on information-processing equipment and software, which accounts for 52.6 percent of business investment spending on total

²⁰ The big surge in new orders in May and June 2005 was largely attributed to unprecedented large orders Boeing received in those two months. After receiving orders for 24 aircraft a month on average for the past two years, Boeing received orders for 200 and 162 aircraft in May and June 2006, respectively. It was the largest orders for any two-month period in Boeing's history. This surge in orders will have a modest impact on business fixed investment over the next few years. For more details, see Macroeconomic Advisers, *Economic Outlook*, July 20, 2005, 10-11.

equipment and software, grew by 13.6 percent in 2004.²¹ It is estimated to have grown 13.1 percent during 2005 and then will likely slow to 9.5 percent during 2006 and 7.8 percent during 2007 as growth in overall economic activity as well as corporate profits are expected to slow down.

Business spending on non-information-processing equipment (i.e., industrial, transportation, and other equipment) started turning around beginning in the second quarter of 2003, after declining for eleven quarters since the second quarter of 2000. It grew 1.1 percent year-over-year during 2003, followed by a healthy 9.8 percent surge during 2004. This non-information equipment spending is estimated to have grown 8.0 percent year-over-year during 2005, and will likely continue to expand 6.6 percent during 2006 and 7.1 percent during 2007.

Business investment spending on total equipment and software is estimated to have grown 10.8 percent during 2005, and will further expand by 8.2 percent in 2006 and 7.5 percent in 2007 (see Figure 15).

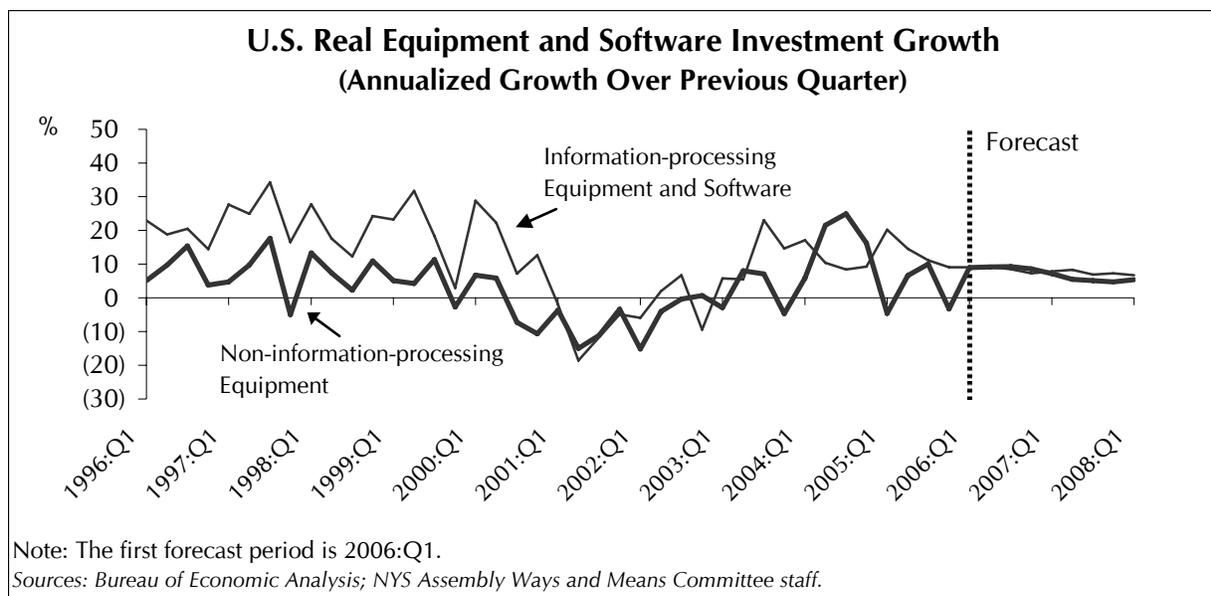


Figure 15

Nonresidential construction spending grew 2.2 percent year-over-year during 2004, after declining for three years in a row. It is estimated to have continued to recover at a year-over-year rate of 1.9 percent during 2005. It will accelerate to 4.0 percent during 2006 as damaged business structures will be rebuilt in the Gulf Coast region and a continued rise in production capacity utilization will put upward pressure on demand for new capacity (see Figure 16). However, as mortgage rates are expected to rise and housing starts are likely to weaken, residential construction spending, which has increased eighteen out of

²¹ The share of 52.6 percent is based on the average of the last five years of data.

nineteen quarters since the third quarter of 2000, is likely to start weakening in 2006 (see Figure 17 and Figure 18). It is forecast to slow to a mere 0.1 percent growth during 2006 and to decline 4.8 percent during 2007 after growing an estimated 7.2 percent year-over-year during 2005.

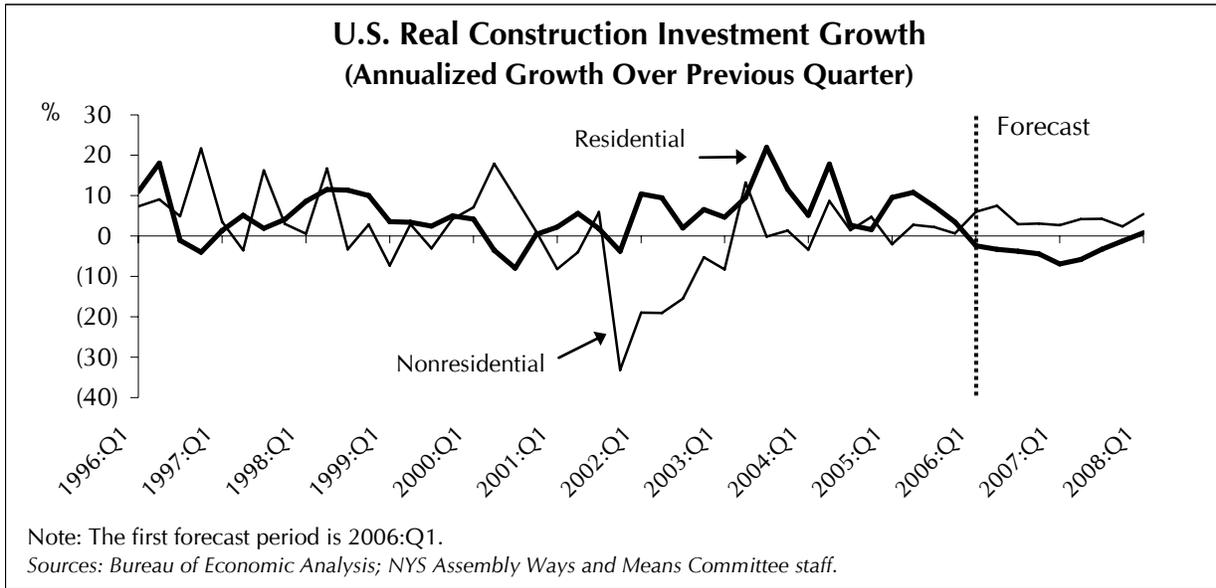


Figure 16

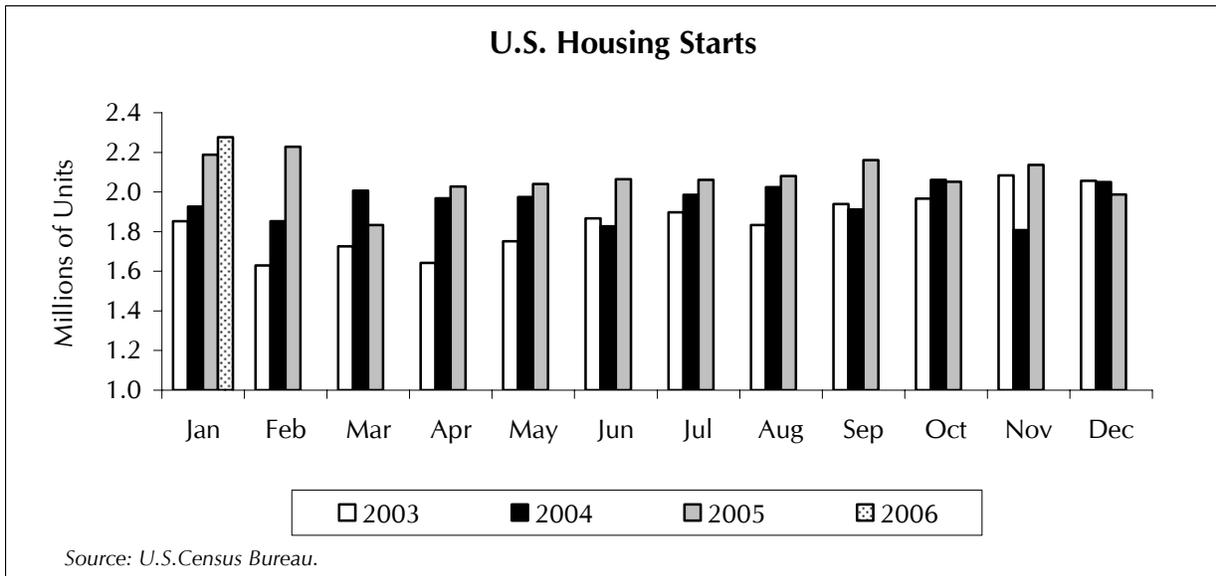


Figure 17

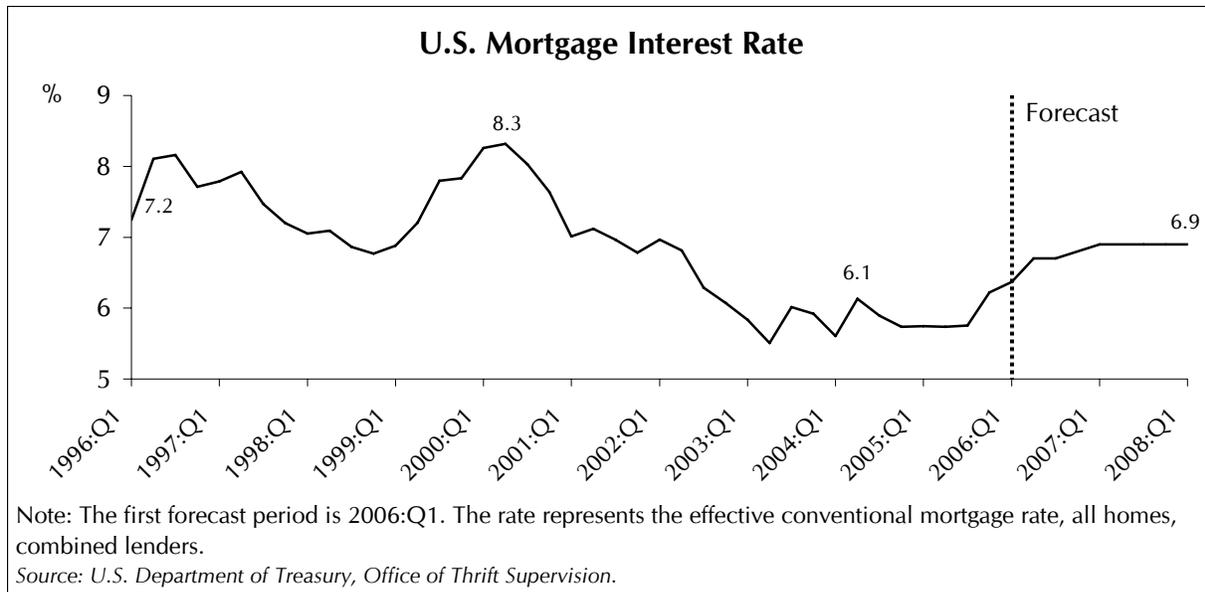


Figure 18

Housing Market

The housing market has given both the State and national economies a big boost over the past several years. Increasing home sales and housing prices have stimulated the economy in two ways. First, housing construction spurs employment and other economic activities. Second, rising real estate values create additional large amounts of wealth for homeowners, the so-called “wealth effect,” which leads to higher household consumption. In the second quarter of 2005 the average home price in the nation increased 13.4 percent compared to the second quarter of 2004. This is the largest annual increase since 1979.²² These facts have caused rising concern about a possible bubble in the housing market. Former Federal Reserve Chairman Alan Greenspan has raised his concerns about the housing market and called the recent boom in the housing market an “imbalance.”²³

In New York State, there is wide disparity in housing affordability across the State. Over the years, some metropolitan areas in the State have become more affordable, while in other metropolitan areas, the opposite has happened. The Housing Opportunity Index, which is defined as the share of homes sold in the area that would have been affordable to a family earning the median income (i.e., the total monthly payment is less than 28 percent of the monthly median household income),²⁴ shows that in the third quarter of 2005,

²² Office of Federal Housing Enterprise Oversight, “House Price Index for the Second Quarter of 2005,” September 1, 2005.

²³ Alan Greenspan, *Reflection on Central Banking*, (symposium sponsored by the Federal Reserve Bank of Kansas City, Jackson Hole, Wyoming, August 26, 2005).

²⁴ For more detail see “What is the NAHB-Wells Fargo Housing Opportunity Index (HOI)?” National Association of Home Builders, September 1, 2005.

Buffalo-Niagara Falls was the most affordable metropolitan area in the State, while New York-White Plains was the least affordable metropolitan area in New York State.²⁵ The percentage of homes sold in the Buffalo-Niagara Falls area that are affordable for a household with median income has risen from 71.3 percent in 1995 to 85.0 percent in 2005. The same affordability percentage has dropped from 33.9 percent to 6.7 percent for New York-White Plains, and from 60.5 percent to 43.2 percent for the nation. During the same period, the ratio of the median price of a new home sold divided by median household income in New York-White Plains rose from 3.7 to 8.1 compared to a drop from 2.1 to 1.5 in Buffalo, and a rise from 2.9 to 4.4 for the nation (see Figure 19).

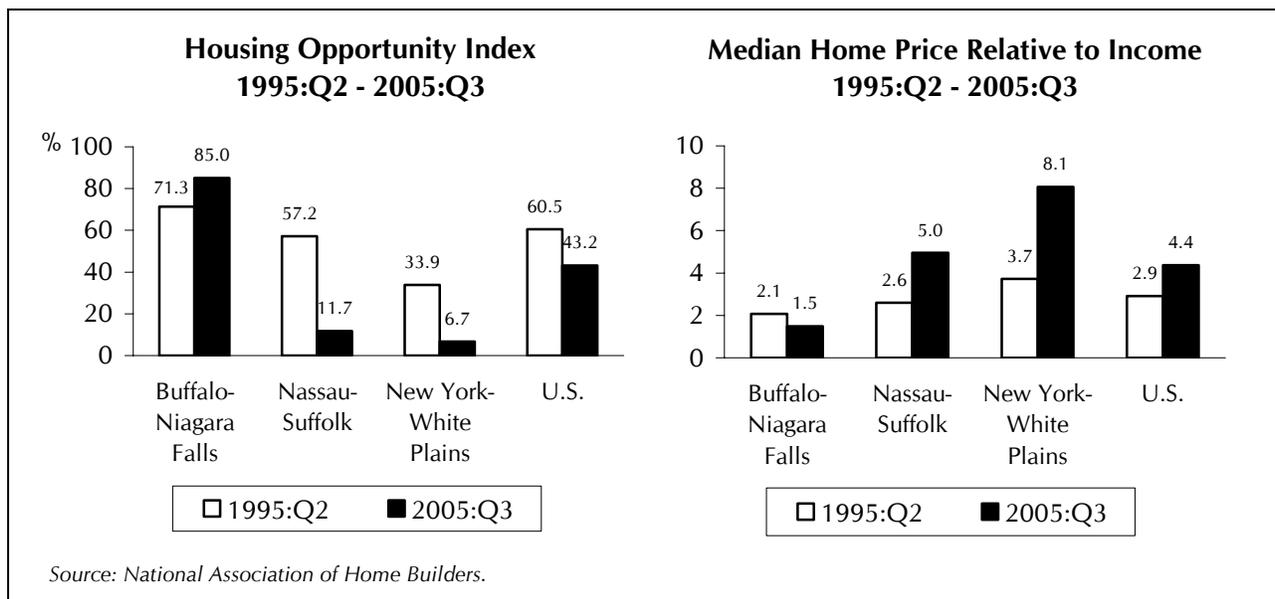


Figure 19

The disparity among metropolitan areas in the State is also seen in the rate of change of housing prices. Several indicators of home price appreciation from 2004 to 2005 reveal a diverse pattern across areas. These indicators include the Office of Federal Housing Enterprise Oversight (OFHEO) Index, which is calculated based on the average housing price changes in repeat sales or refinancing of single-family properties.²⁶ Although house prices in New York State grew at a similar rate compared with the nation, there are several areas that prices have grown much differently from the rest (see Table 2).

²⁵ "Wells Fargo Housing Opportunity Index," National Association of Home Builders, August 25, 2005.

²⁶ For more detail see Charles A. Calhoun, Department of Housing and Urban Development, *Office of Federal Housing Enterprise Oversight*, "OEHEO House Price Indexes: HPI Technical Description," March 1996.

Table 2

Home Price Appreciation New York State, State Metropolitan Areas, and U.S. From 2004:Q3 to 2005:Q3			
	OFHEO Home Price Index	Median Price of Existing Homes Sold	Median Price of New Homes Sold
Albany-Schenectady-Troy	14.6 %	14.2 %	N/A
New York-White Plains	13.6	20.0	27.4 %
Nassau-Suffolk	12.6	12.8	6.8
Syracuse	7.3	14.8	N/A
Buffalo-Niagara Falls	5.9	1.6	(10.5)
Rochester	5.2	5.3	0.9
NYS	11.9	N/A	N/A
U.S.	12.0	13.3	12.4

Sources: Office of Federal Housing Enterprise Oversight; National Association of Home Builders; Freddie Mac; and the National Association of Realtors.

There are several reasons for housing price increases, such as a change in fundamental factors like a strong economy that leads to higher family income, higher demand from an increased population, and low mortgage rates. The 30-year conventional mortgage fixed-rate has declined from 9.15 percent in January 1995 to 6.15 percent in January 2006.²⁷ There is greater availability of nontraditional mortgages such as balloon payment mortgages or interest-only loans which allow homeowners to reduce their initial payment. As a result, the buyer has an increased chance of qualifying for credit, which in turn boosts demand for housing.²⁸ In 2003, about one percent of homes with at least one mortgage are using balloon mortgage, compared to less than 0.8 percent in 1999.²⁹ Even without significant changes in demand and supply, housing prices may still rise as a reflection of rising investment and speculative activities. Twenty-three percent of all homes purchased in 2004 were for investment.³⁰

²⁷ Federal Reserve Statistical Release, Selected Interest Rates, <http://www.federalreserve.gov/releases/h15/current>. (February 13, 2006).

²⁸ Balloon payment mortgage is a short-term fixed rate that usually requires smaller payment for a certain period and one large payment for the entire amount of the outstanding principal. Interest-only loan is the loan that borrowers pay only interest for a specific period and pay higher payments once the interest-only period ends.

²⁹ U.S. Census Bureau, *American Housing Survey for the United States: 1999 and 2003*, Mortgage Characteristics – Owner Occupied Units, Table 3-15. <http://www.census.gov/prod/2004pubs/H150-03.pdf>, <http://www.census.gov/prod/2000pubs/h150-99.pdf>. (Issued September 2004).

³⁰ "Second-Home Market Surges, Bigger Than Shown in Earlier Studies," National Association of Realtors, March 1, 2005.

Elevated housing prices not only impact affordability, but also affect the labor market in the area. High housing prices in Long Island is one of the possible causes of out-migration of young college-educated workers from the region. During the 1990s, Long Island lost about 20 percent of its young working-age population (18- to 34-year-olds), while a current survey found that 70 percent of residents from this age group said that they are somewhat or very likely to leave in the next five years.³¹ This probably contributed to the slow job growth in the area.

In recent years, more households have chosen to use Adjustable-Rate Mortgage (ARMs) rather than fixed rate loans to finance their home. It is estimated that about 36 percent of new loans are financed using ARMs.³² As a result, any changes in mortgage interest rates could impact those households as well as the economy. If the mortgage interest rate keeps rising, homeowners may find they can no longer afford their homes.

Home price appreciation in metropolitan areas within the State as well as the national average began to moderate in the third quarter of 2005. It is expected that activity in the housing market as well as home prices will gradually slow in the near future. Mortgage rates are expected to rise, thus weakening the affordability as well as the demand for housing. Regulators and mortgage bankers are increasingly concerned about the potential future default risk of using nontraditional mortgages. This may cause mortgage lenders to be more selective with their lending, which will lead to a lower demand due to higher borrowing costs. In addition, investors may become less willing to purchase groups of mortgage loans packaged and sold in financial markets.

Government

Federal Government Spending

In constant dollars, federal government spending is expected to grow 1.4 percent in 2006 and 1.1 percent in 2007 (see Figure 20). In 2006, the defense spending in Iraq and Afghanistan will continue to contribute to federal spending growth. The largest increase in spending, however, will be due to the relief and reconstruction spending in the Gulf Coast region. There is considerable uncertainty on the extent of federal government expenditures necessary for efforts in the regions affected by the hurricanes. An estimate of the increase in federal spending places the federal relief and reconstruction spending at \$212 billion.³³ Though this spending will be spread over many years, it is worth noting that it accounts for about eight percent of the expected 2005 fiscal year federal government spending of

³¹ "Long Island Index 2005," page 4; and "Long Island Index 2006," page 15; see <http://www.longislandindex.org/fileadmin/reports/2005LongIslandIndex.pdf>; and <http://www.longislandindex.org/fileadmin/reports/INDEX2006a.pdf>

³² Albert B. Crenshaw, "Homeowners in Harm's Way," *Washington Post*, April 3, 2005.

³³ U.S. Congressional Budget Office, *The Macroeconomic and Budgetary Effects of Hurricanes Katrina and Rita: An Update*, September 29, 2005.

\$2.5 trillion.³⁴ So far a spending package of \$62 billion has been allocated to cover relief efforts.³⁵

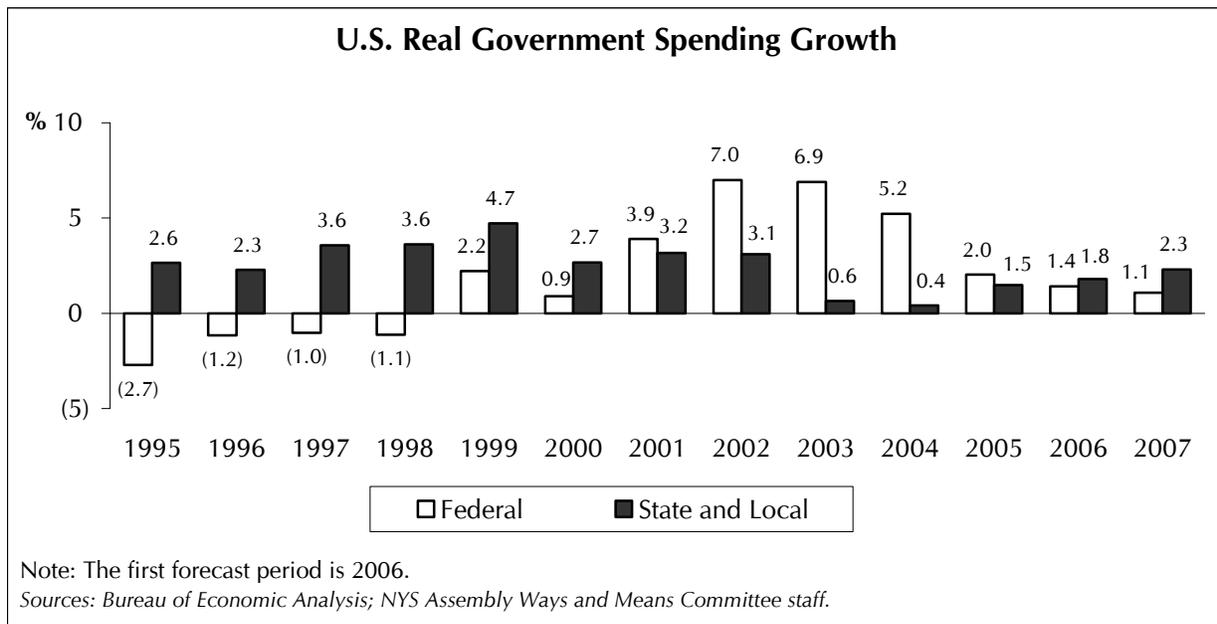


Figure 20

Since business investment has revived, we can expect countercyclical government spending to fall. The fiscal year 2005 federal budget deficit is \$318.6 billion, which is much smaller than the \$394 billion deficit that was expected in March 2005.³⁶ This improvement was largely on account of an unexpected increase in revenue of over \$100 billion. An improving economy has contributed to this increase in revenue, and both personal and corporate incomes have grown at fast rates. The strong housing market and changes in tax policy are also argued to have had an impact on revenue through an increase in capital gains.³⁷ Despite improving revenues, it is expected that increased federal spending due to the recent hurricanes and other natural disasters will require cuts in other spending: H.R. 3966 is intended to enable the president to request that Congress consider such spending reductions. Over longer horizons, expected spending on social security, Medicare, and Medicaid may force a rethinking of budget priorities.

³⁴ This estimate was made before Hurricane Katrina: U.S. Congressional Budget Office, *Budget and Economic Outlook: An Update*, August 2005, slides.

³⁵ "Macroeconomic and Budget Effects of Hurricanes Katrina and Rita," (CBO Testimony: Statement of Douglas Holtz-Eakin before the Committee on the Budget, U.S. House of Representatives, October 6, 2005.)

³⁶ Paul Blustein, "Federal Deficit Fell in the Past Year," *Washington Post*, October 15, 2005; U.S. Congressional Budget Office, *The Budget and Economic Outlook: Fiscal Years 2007 to 2016*, January 2006.

³⁷ Mark Zandi, "Who Gets Credit For Falling Federal Deficit?" *Moody's Economy.com, Dismal Scientist*, <http://www.economy.com/dismal/pro/article.asp?cid=15989> (July 13, 2005).

State and Local Government Spending

State and local government spending is expected to grow 1.8 percent in 2006 and 2.3 percent in 2007 in constant dollars. State and local government spending was affected by the cyclical loss of revenue after the 2001 recession and will continue to recover from the economic downturn, while Medicaid will remain the engine of expenditure growth.³⁸ While most state and local governments cut their spending growth in response to fiscal conditions, aggregate state expenditures grew at a rate close to the long-term state spending trend of 6.4 percent, due to other expenditures such as one-time spending from surplus funds, other reserve funds, and the Federal Fiscal Assistance Package.

State and local government spending growth is expected to improve in 2006 and 2007, on account of continuing improvement in revenue from all major tax types as well as the improvement in the near-term economic outlook. In the third quarter of 2003, the combined state and local government revenues from personal income tax, the corporate income tax, and sales tax rose for the first time since 2000.³⁹ In the fourth quarter of 2004, states experienced the strongest fourth-quarter revenue growth from taxes since 1991.⁴⁰ After adjusting for inflation and legislated tax changes, average growth in state tax revenue in 2004 was the strongest since 1998.⁴¹ State tax revenue is expected to slow down but remain healthy throughout the next two fiscal years. State net taxes and fees will increase by \$2.5 billion in fiscal year 2006, the fifth consecutive year of net tax increases. Revenue from sales tax, personal income tax, and corporate income tax is expected to continue to grow for fiscal years 2006 and 2007 as general economic conditions continue to improve.⁴²

Exports and Imports

The Assembly Ways and Means Committee staff forecasts that, in constant dollars, exports will grow 6.1 percent in 2006 and 6.9 percent in 2007 after rising 6.7 percent in 2005. With the U.S. economy expected to grow faster than the rest of the world, imports are forecast to grow 5.4 percent year-over-year in 2006 and 4.6 percent in 2007, following 6.2 percent growth in 2005 (see Figure 21). Net exports, defined as exports minus imports, have declined (becoming more negative) every year since 1995, adversely affecting GDP. This trend is expected to continue in 2006 and 2007. Although exports will grow faster than imports in 2006 and 2007, net exports is likely to continue to decline during this

³⁸ Donald Boyd, "New Census Data Offer Glimpse of States' Early Responses to the Fiscal Crisis," *State Fiscal Brief*, no. 73, Nelson A. Rockefeller Institute of Government, April 2005, 4.

³⁹ U.S. Congress, Congressional Budget Office, *The Budget and Economic Outlook: Fiscal Year 2005 to 2014*, January 2004, Box 2-1, 36.

⁴⁰ Nicholas W. Jenny, "State Tax Revenue Ends 2004 in Solid Shape," *State Revenue Report*, no. 59, Nelson A. Rockefeller Institute of Government, March 2005, 1.

⁴¹ *Ibid*, table 1.

⁴² *Précis Macro*, Moody's Economy.com, January 2006.

period. This is because the base level of imports is about 50 percent higher than the level of exports. For example, in 2005 real exports were \$1.2 trillion while real imports were \$1.8 trillion. Therefore, exports must increase at a much higher percentage rate than imports just to keep net exports from declining.

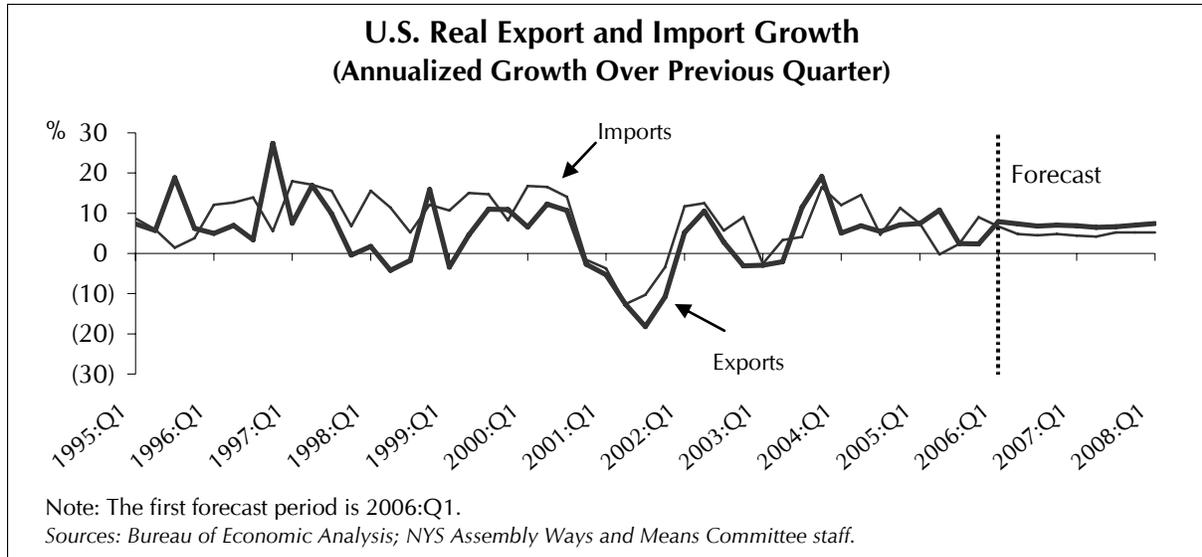


Figure 21

During most of the recovery following the 2001 recession, the value of the dollar was generally falling. However, in the second quarter of 2005 the dollar briefly regained strength. It is expected the dollar will resume its gradual decline in 2006 (see Figure 22). The decline of the dollar during much of the recovery was a positive factor for net exports, helping to boost exports and reduce imports. However, the dollar's decline can hurt the prices of United States assets. In addition, a declining dollar can cause increased inflation. This is partly because imported goods become more expensive. In addition, the increased prices of competing imports in dollars reduce the pressure on domestic manufacturers to keep prices down.

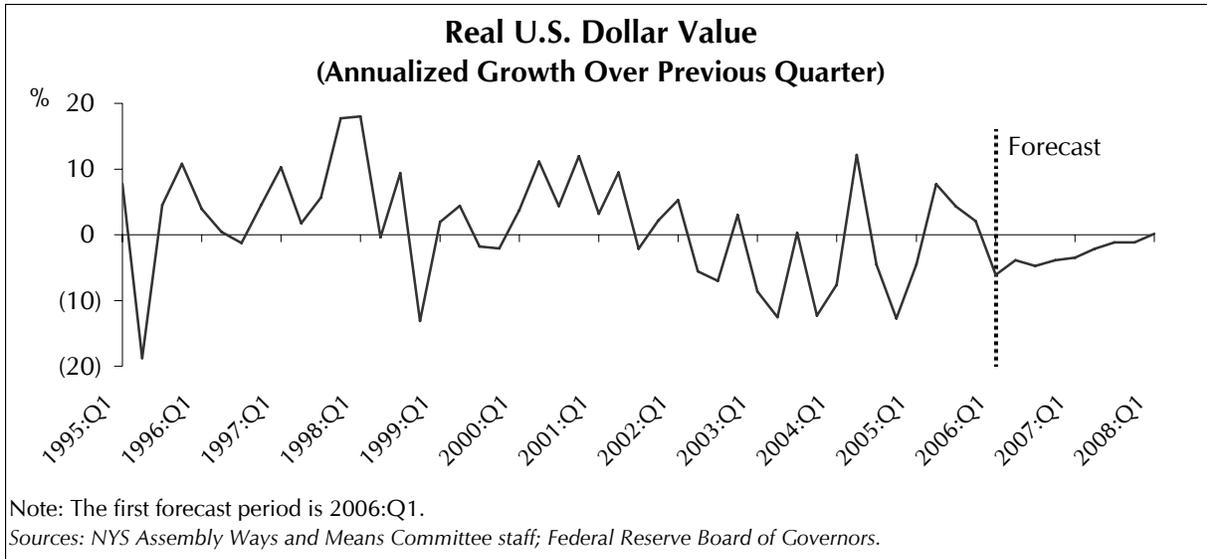


Figure 22

The decline of the dollar is being driven in large part by the growing current account deficit, which reached a record high of \$794.7 billion in the first quarter of 2005 (see Figure 23). Net imports, the current account, and the budget deficit are likely to decline in 2006 and 2007. The impact on both the current account and the budget deficit is expected to cause the dollar to continue to decline in 2006 and 2007. Former Federal Reserve Chairman Alan Greenspan, who in the past had argued that the current account deficit is not as serious an issue as some economists have suggested,⁴³ raised his own concerns in an August 2005 speech about the long-term consequences of persistent current account deficits and mentioned that it needs to be dealt with in greater detail than in the past.⁴⁴

⁴³ See for example: Alan Greenspan, "The Evolving U.S. Imbalance and Its Impact on Europe and the Rest of the World," *Cato Journal* 24, spring/summer 2004, 1-11.

⁴⁴ Alan Greenspan, *Reflection on Central Banking* (symposium sponsored by the Federal Reserve Bank of Kansas City, Jackson Hole, Wyoming, August 26, 2005).



Figure 23

On July 21, 2005, the Chinese government decided to abandon its fixed exchange rate and move to a managed float system, which pegs the yuan against a basket of major currencies instead of the U.S. dollar. The change led immediately to a 2 percent appreciation of the yuan relative to the dollar. U.S. trade with China accounted for 12 percent of total U.S. trade value. A ten percent appreciation of the yuan relative to the U.S. dollar will result in approximately a 1.2 percent appreciation of U.S. dollars on a trade-weighted basis. The yuan will need a substantial reevaluation to have a significant impact on prices, consumption, imports, and exports, as well as economic growth for both China and the United States.

It is expected that the yuan will continue to appreciate at the rate of 5 to 10 percent a year for the next few years. According to Global Insight, if the yuan appreciates at a rate of 5 percent and all other Asian countries allow their currencies to appreciate by nearly the same amount; this will translate into about a four percent depreciation of the dollar on a trade-weighted basis in the next two years. Under these conditions, the dollar would then decline further by about eight percent over the next four years. It is predicted that this depreciation could improve the U.S. growth rate by 0.2 to 0.3 percentage point annually, while adding 30 to 50 basis points to the long-term bond yield over the next few years.⁴⁵

The current forecast assumes that although the dollar may decline, it will not suffer the dramatic collapse some economists fear during the forecast period. Therefore, the stronger yuan and a decline in the dollar will have a positive impact on GDP by raising exports and reducing imports. In addition, a strong global economy will help to improve exports.

⁴⁵ "U.S. Executive Summary," Global Insight, August 2005.

World GDP growth is expected to remain above 3.0 percent in both 2006 and 2007. Developed nations are all expected to have positive growth in 2006 according to a poll of forecasters taken by the *Economist*.⁴⁶ However, according to the poll, the United States is expected to grow faster than any other developed nation in 2006. Europe is expected to grow 1.9 percent in 2006, while Canada, the largest trade partner for the United States, is expected to grow 3.1 percent. Japan is expected to continue having positive growth after years of stagnant economic performance, with growth of 2.5 percent in 2005 and 2.4 percent in 2006.

Much of the developing world is experiencing rapid growth. China has been a focus of considerable attention, with growth in the fourth quarter of 2005 at 9.9 percent. The Chinese government has been acting to slow growth to a more controlled pace. Some other Asian countries are also growing rapidly, including India and Malaysia. Some South American countries are also expanding rapidly, with 9.8 percent GDP growth in the third quarter of 2005 for Venezuela.

With economic activity worldwide expanding for nearly all of our significant trading partners, the global economy will be a positive stimulus for the United States economy.

Employment

United States employment shows a profile of strengthening employment growth in 2004 and stable employment growth in 2005 and beyond (see Figure 24). After growing 1.5 percent in 2005, it is expected that employment will grow 1.5 percent in 2006 and 2007. It is expected that there will be 2.0 million more jobs in both 2006 compared to 2005. The largest additions to employment in 2006 are expected to be in education and health, other services, and construction. All sectors will experience an increase in employment in 2006. Employment is estimated to have increased in all sectors except manufacturing and information in 2005.

⁴⁶ "Economic and Financial Indicators," *Economist*, January 28-February 3, 2006, 100.

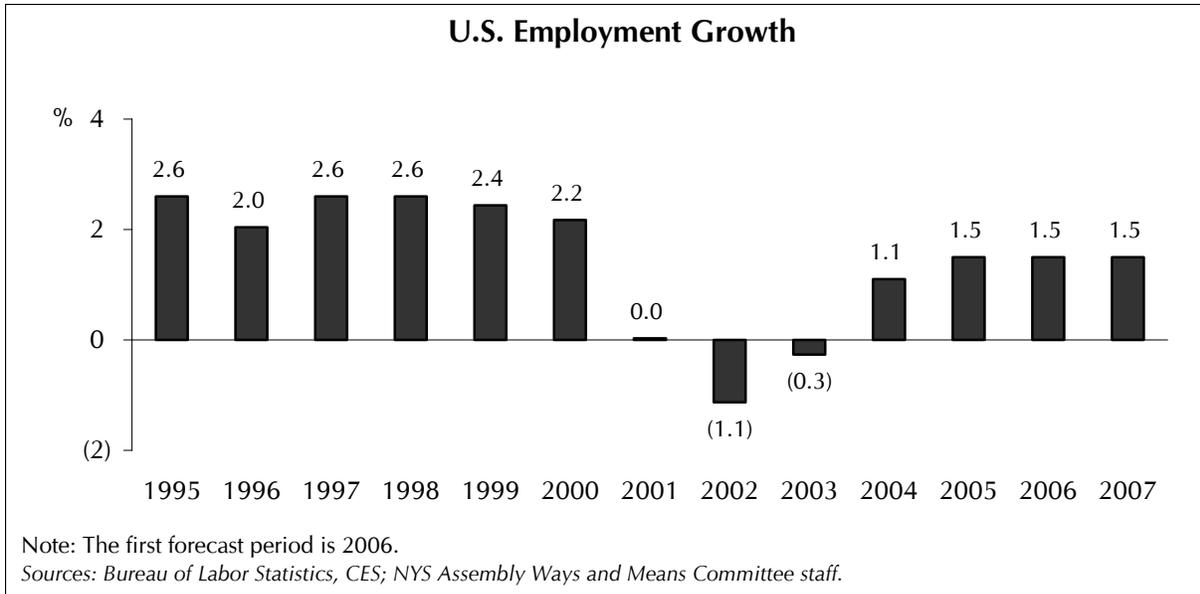


Figure 24

Since the largest loss of jobs from the 2001 recession was in manufacturing, a fall in the rate of loss of manufacturing jobs will contribute greatly to the employment expansion. (see Figure 25). The fastest rate of growth in employment among the sectors in 2006 is expected to be in construction, which partly reflects the increase in the demand for construction in the Gulf Coast region reconstruction effort (see Table 3). The fast growth of professional services reflects the increased demand for producer services in the employment expansion. The steady growth in the demand for education and health services will also contribute significantly to job growth in 2006.

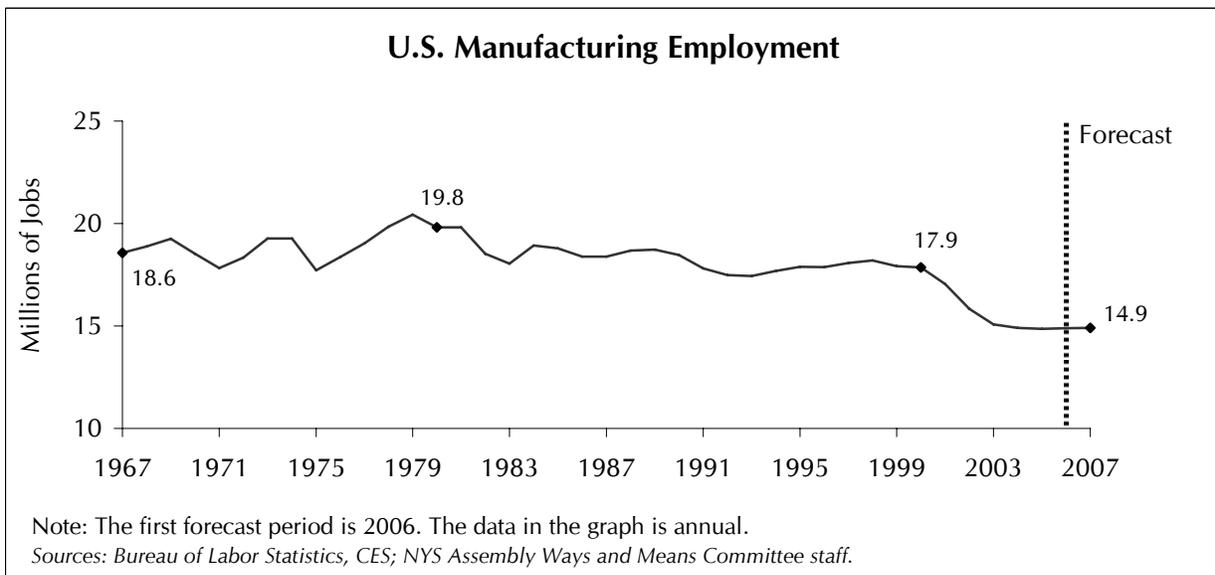


Figure 25

Table 3

U.S. Employment by Sector				
(Percent Change)				
	Actual	Estimate	Forecast	Forecast
	2004	2005	2006	2007
TOTAL	1.1	1.5	1.5	1.5
Government	0.2	0.9	0.6	0.7
Education and Health	2.2	2.3	2.2	2.2
Retail Trade	0.9	1.3	1.2	1.6
Manufacturing ¹	(1.2)	(0.3)	0.2	0.1
Other Services ²	1.8	1.5	2.2	2.1
Leisure & Hospitality	2.6	2.4	1.3	1.6
FIRE ³	0.7	1.4	2.2	1.5
Construction	3.6	4.4	3.7	1.9
Wholesale Trade	0.9	1.5	1.5	1.5
Professional Services	2.2	3.5	2.9	2.5
Transp. & Utilities ⁴	1.0	1.9	1.7	1.9
Information	(2.2)	(1.7)	0.3	0.6
Mgmt. of Companies	2.2	1.6	0.6	1.2

¹ Including Mining and Logging.
² Including Administrative, Support, and Waste Management Services.
³ Financial Activities including Finance, Insurance, Real Estate, Rental, and Leasing.
⁴ Transportation, Warehousing, and Utilities.
Sources: Bureau of Labor Statistics, CES; NYS Assembly Ways and Means Committee staff.

The Assembly Ways and Means Committee staff's forecast for labor productivity for 2006 is 2.5 percent (see Table 1 on page 15). Figure 26 shows how labor productivity growth has varied since 1966. The considerable variability in labor productivity is influenced by cyclical macroeconomic conditions. The figure also shows how labor productivity typically falls during the initial stages of a recession, since output falls faster than employment in an economic slowdown; labor productivity also increases sharply after a recession since output recovers faster. In the recent recession, employment decline and recovery were spread over a longer period of time compared to previous recessions (see Figure 1 on page 1).

Apart from cyclical variations in labor productivity, there has been an increase in the rate of growth in labor productivity in the 1990s, compared to the late 1970s and the 1980s. This is widely attributed to the falling price of computer hardware and the increase in the extent of information technology use.⁴⁷ The Committee staff's forecast is based on

⁴⁷ Dale Jorgensen, Mun S. Ho, and Kevin J. Stiroh, "Will the U.S. Productivity Resurgence Continue?" *Current Issues in Economics and Finance*, 10 (3), December 2004.

the expectation that this long-run tendency will continue to keep labor productivity growth high in the next few years.⁴⁸

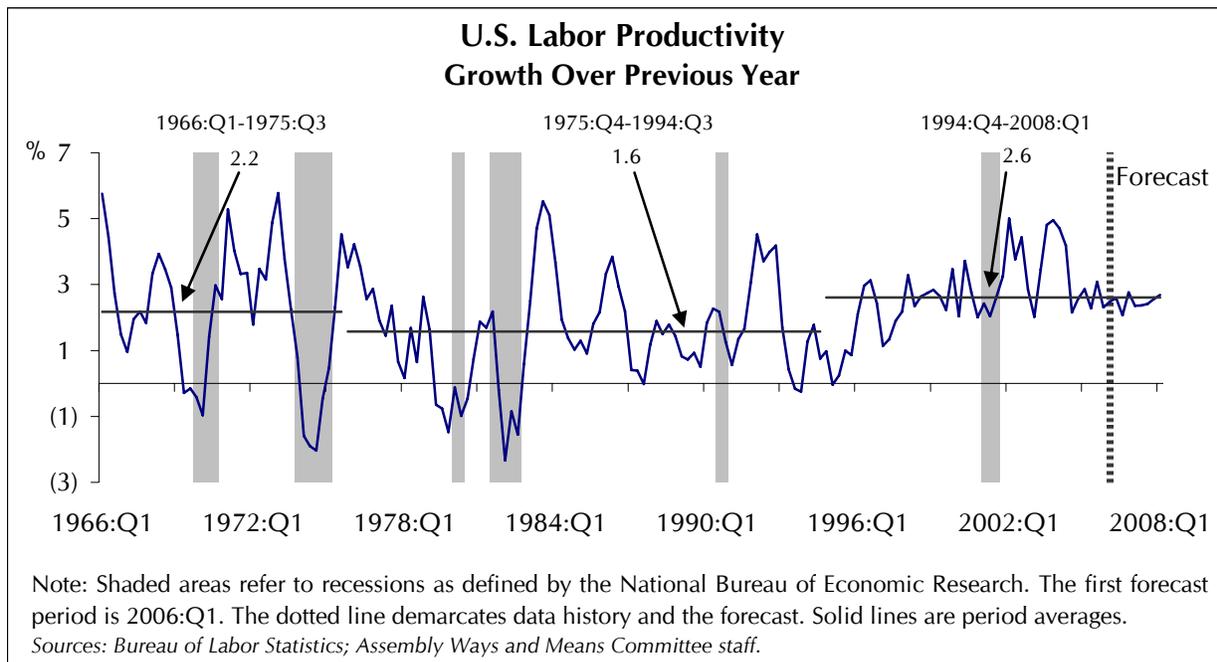


Figure 26

Personal Income

The Ways and Means Committee staff forecasts that most of personal income components are expected to remain strong or grow faster than previous years. Personal income grew 5.9 percent in 2004 after an increase of 3.2 percent in 2003. It is estimated to have further grown 5.4 percent in 2005, and is forecast to grow another 6.1 percent in 2006 and 5.7 percent in 2007 (see Figure 27).

⁴⁸ In "The 'New Economy': Post Mortem or Second Wind?" *Journal of Economic Perspectives*, 16(2), spring 2002, Martin N. Baily argues that the trend growth rate of labor productivity is between 2.2 and 2.7 percent. Dale W. Jorgensen and others expect that labor productivity will grow 2.6 percent per year in the 2004-14 period. See Dale W. Jorgensen, Mun S. Ho, and Kevin J. Stiroh, op cit.

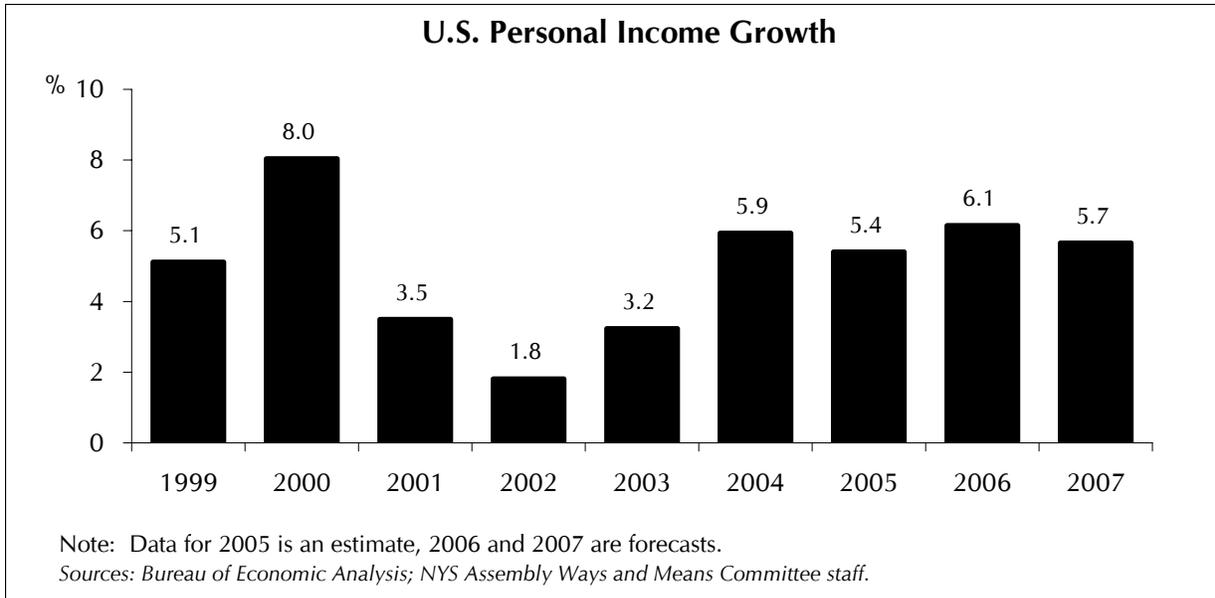


Figure 27

Wages and salaries income is the largest component of total personal income. It accounted for around 55 percent of personal income in 2004. This component grew 5.4 percent year-over-year during 2004, and grew strongly at 6.0 percent in 2005. Wages and salaries growth is expected to slow to 5.4 percent in 2006, as growth in both employment and wage rates are expected to slow a bit from 2005. Wages will grow 5.3 percent in 2007.

Dividend income grew 4.3 percent in 2005. As corporate profits are expected to continue to grow, dividend income will also likely continue to grow 9.3 percent in 2006 and 6.8 in 2007. The seemingly strong growth in dividend income in 2006 is in part due to the fact that 2005 growth was pushed lower by the Microsoft one-time dividend payout of \$32.4 billion on December 2, 2004.

With more interest rate hikes expected, interest income is forecast to continue to increase 6.6 percent year-over-year in 2006. In 2007, as interest rates are expected to stay steady, interest income will grow at 5.2 percent.

Rental income, a relatively small portion of total personal income, is estimated to have dropped significantly by 44.9 percent in 2005, mainly due to property loss from hurricanes Katrina and Rita. Rental income is forecast to grow 18.2 percent in 2006.

Transfer income is expected to increase by 6.7 percent in 2006 compared to 6.9 percent in 2005. Unemployment is expected to decline throughout the forecast period, therefore personal unemployment insurance receipts will decline. However, Medicare benefits will increase because of the new prescription drug plan.

Income Inequality

Average incomes in the United States have been rising long-term. However, income inequality has been rising as well. Incomes have diverged, with poorer households experiencing less income growth across almost all time periods (see Figure 28). In the thirty-year period from 1974 to 2004, mean real income has gone up 2.0 percent a year for the richest five percent of households and 1.5 percent a year for the richest 20 percent of households. However, real incomes for the poorest 20 percent of households have gone up a relatively small 0.3 percent a year. These poorest 20 percent of households increased their income by an amount that is only 20.7 percent of the increase for the richest 20 percent of households. It should be noted that the “real” income is adjusted based on the consumer price index (CPI) which uses the typical basket of goods consumed by all households. If poor households devote a higher percentage of their income to items such as rent and medical care, which increase faster than the CPI in general, then their real income gains may have been even weaker or even negative. Recent events such as skyrocketing energy prices and hurricanes also disproportionately impact low-income groups. High prices for basic necessities such as natural gas or heating oil have a larger negative impact for the poorest households. Deaths, forced relocation, and other losses from hurricanes have also particularly hurt low-income households.

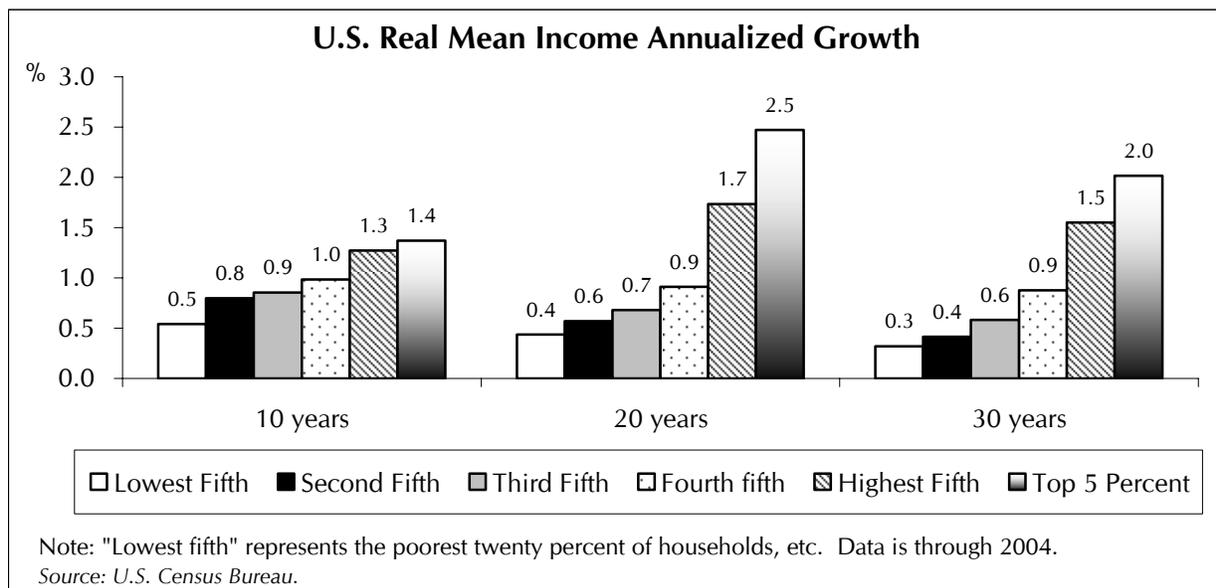


Figure 28

The ratio of high-income to lower percentile categories shows a similar trend. In 1974, the 20 percent of households with the highest income made 10.3 times as much as the poorest 20 percent. By 2004 they made 14.8 times as much (see Figure 29).

Wage earners in general are also benefiting less from the current economic expansion. Companies are paying less of their cash gains in the form of wages and salaries

than they have at any time since the Great Depression.⁴⁹ Furthermore, the growth in compensation for employees of corporations has been the slowest it has ever been in any expansion of equal length in the past fifty years. Therefore, not only have incomes diverged, but the portion of national output that is going to rewarding investors has increased at the expense of output going to wage earners.

Corporate wealth has also become more concentrated according to data from the Congressional Budget Office. The top one percent of households owned 57.5 percent of corporate wealth in 2003, up substantially from 53.4 percent in 2002 and 38.7 percent in 1991.⁵⁰

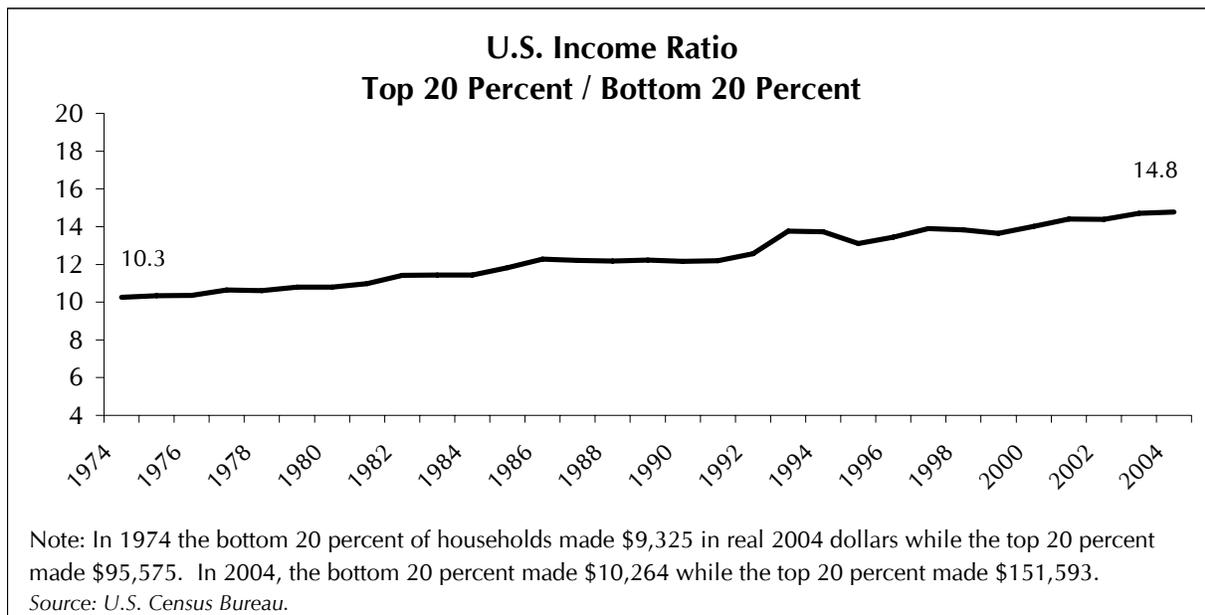


Figure 29

In New York State, incomes for poor and rich households have diverged even more than at the national level. According to data from the Fiscal Policy Institute, real income in New York State rose a modest 0.6 percent annually for the poorest fifth of families between 1980 to 1982 and 2001 to 2003 while income for the richest fifth of families jumped 3.1 percent annually (see Figure 30). In addition to growing inequality, the gap between the richest fifth and the poorest fifth is higher in New York State than in any other state in the nation.⁵¹

⁴⁹ Nicholas Johnston and Alison Fitzgerald, "Bush's Expansion Leaves Workers Behind, Sparking Fed Friction," *Bloomberg*, January 17, 2006.

⁵⁰ David Cay Johnston, "Corporate Wealth Share Rises for Top-Income Americans," *New York Times*, January 29, 2006.

⁵¹ Fiscal Policy Institute, "Pulling Apart in New York: An Analysis of Income Trends in New York State," January 26, 2006.

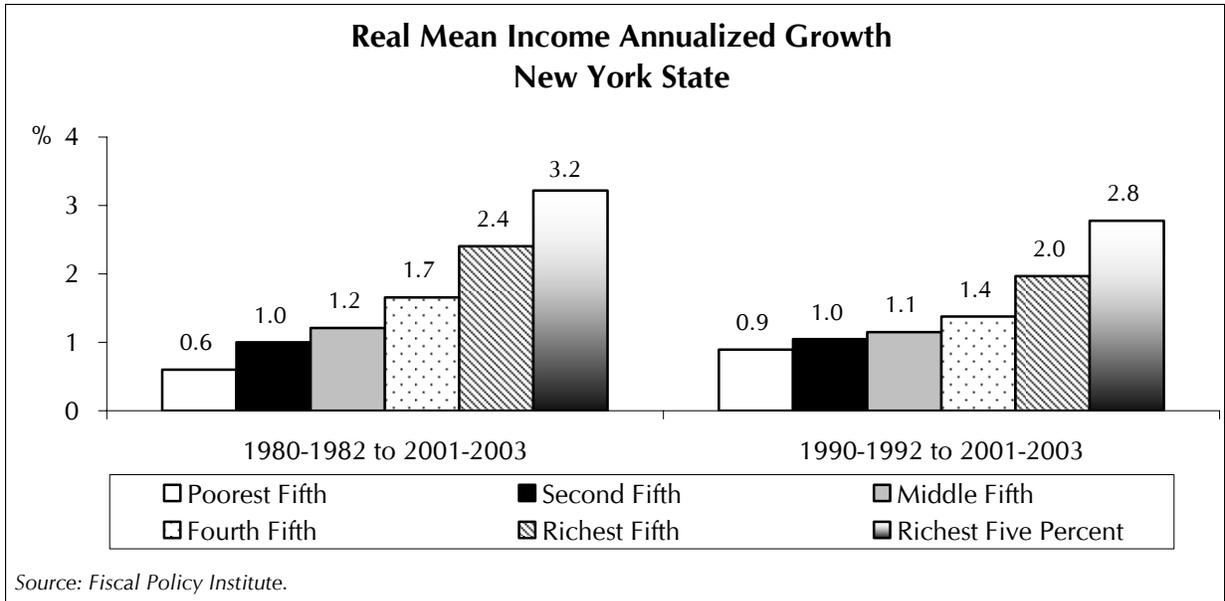


Figure 30

The increasing disparity of income is also apparent regionally within New York City. Income growth in Manhattan, the richest borough, has outpaced the nation in recent years. Meanwhile income growth in the other four boroughs has not only underperformed the nation, it has not even kept up with inflation.⁵²

Prices

Increases in consumer and producer prices in 2004 were driven by volatile energy prices, and this continued into 2005. A sustained increase in oil prices led to near-record high gasoline prices in 2005. A drastic increase in gasoline prices was seen as a result of Hurricane Katrina, which affected the Gulf Coast where much of the nation's gasoline is refined (see the Economic Impact of Recent Hurricanes section on page 5). Rising energy prices in 2004 and 2005 have also contributed to increases in raw materials prices for producers.

Besides energy, other factors contributing to the inflation picture include slower growth in productivity and strong wage growth. Also, the weak dollar continues to put upward pressure on prices (import prices in particular).

The growth of the core CPI (CPI excluding food and energy) has been less volatile than the growth of the overall CPI (see Figure 31). Although core prices have been rising, they have not been subject to the volatility of energy prices.

⁵² Jennifer Steinhauser, "As Manhattan Booms, Inflation Squeezes Rest of New York," *New York Times*, January 25, 2006.

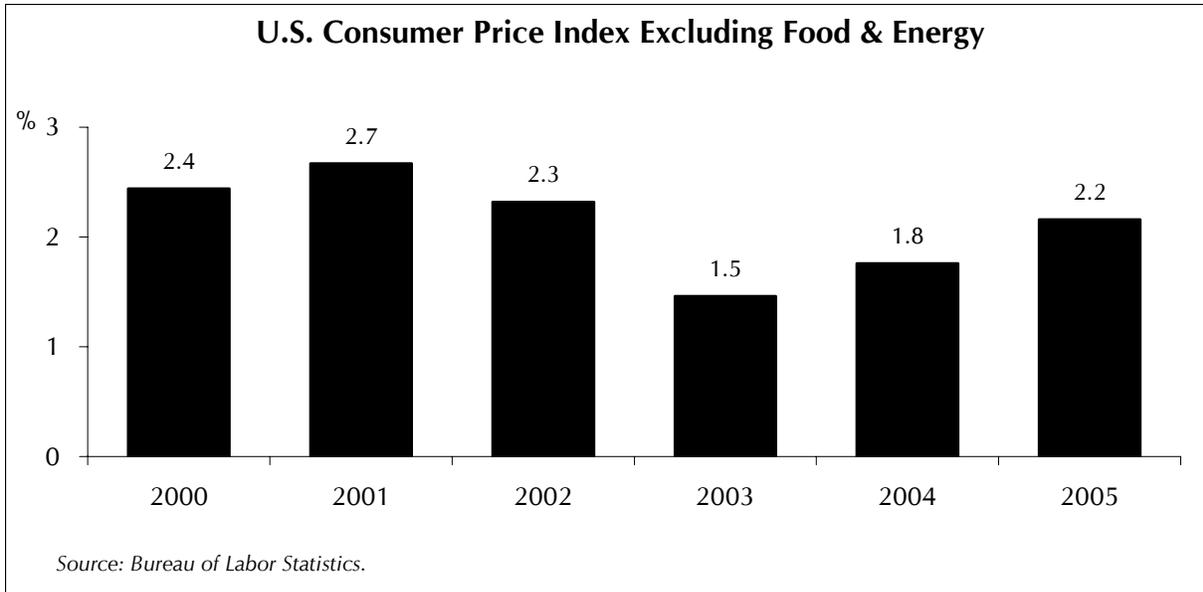


Figure 31

The Assembly Ways and Means Committee staff predicts that the general price level, as measured by the Consumer Price Index (CPI), will increase 3.2 percent year-over-year in 2006 following growth of 3.4 percent in 2005 (see Figure 32). In 2007, the general price level will increase by 2.7 percent.

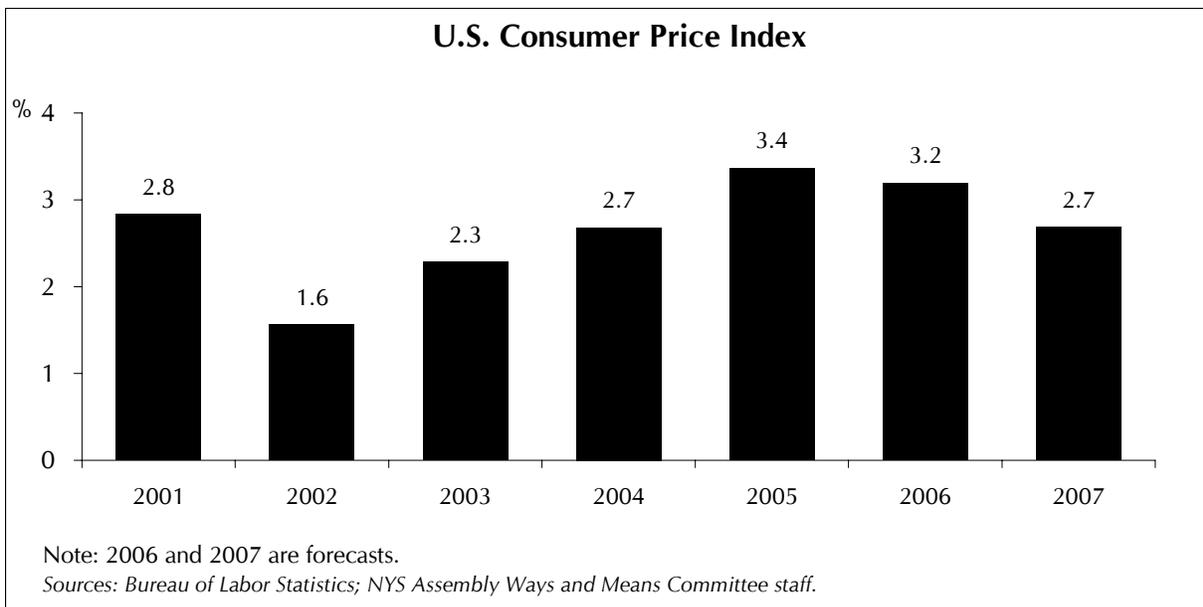


Figure 32

Although energy prices have been a major component of rising inflation recently, oil prices are expected to stabilize in 2006 and 2007. As other underlying fundamentals are also stable, upward pressure on the CPI should abate. Also, the overall forecasted

slowdown in the general economy is reflected in the lower expected CPI growth for 2006 compared to 2005.

Oil and Energy Prices

Energy prices continue to remain a critical issue for the United States economy. Energy prices generally are more variable than other prices, and the past few years have been no exception. Trading floor reaction to current political and geographical considerations continue to add uncertainty to future energy prices, including prices of oil, gasoline, and natural gas. Weather patterns also affect energy supplies and prices. General uncertainty surrounding the energy markets has also pushed up the price of crude futures.

The price of oil (as measured by the U.S. refinery's average acquisition price of imported oil) has increased in the past two years. This is due to many factors, including production constraints, dramatic growth in demand, weather-induced disasters, the War in Iraq, political and labor unrest in oil producing countries, uncertainty in the market, and speculation on the part of investors. However, if the price of oil is adjusted for inflation, oil prices are not as high as in the early 1980s (see Figure 33). The 2006 nominal price of oil would have to reach almost \$89 per barrel to surpass the record set in January of 1981 (monthly data).

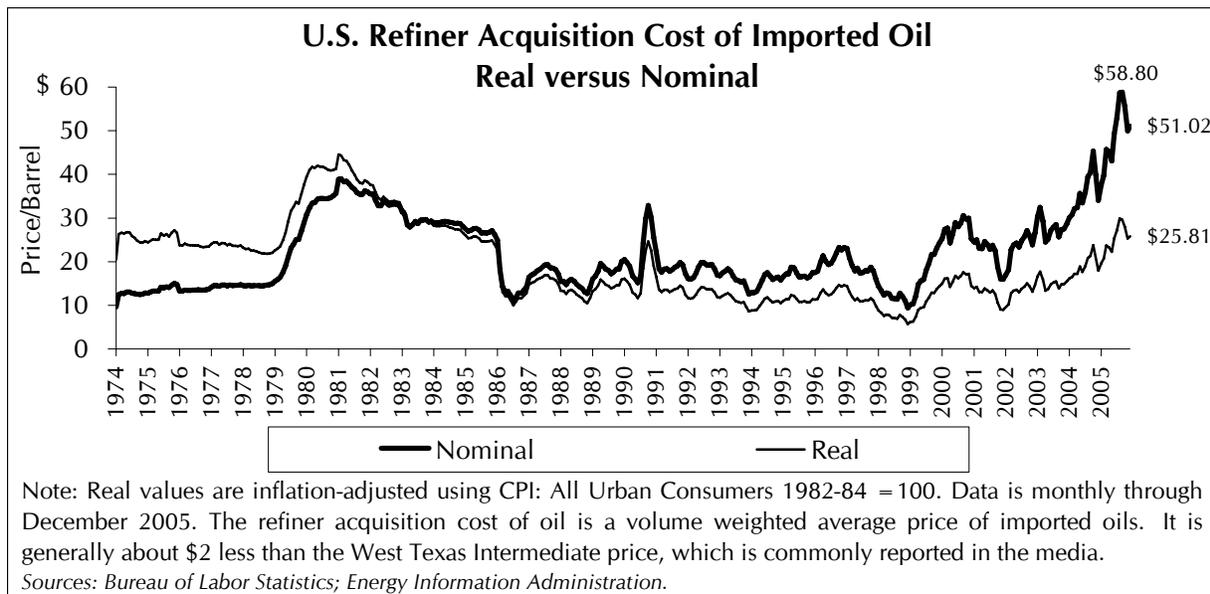


Figure 33

The sharp rise in oil prices have has produced record profits for oil companies. Many of the companies have reported record profits and revenues. Exxon Mobil reported profits of \$36.13 billion in 2005, the most ever for an American company.⁵³

⁵³ Simon Romero and John Holusha, "Exxon Mobile Posts Largest Annual Profit for U.S. Company," *New York Times*, January 30, 2006.

Crude oil contributes 55 percent of the price of a gallon of gas; therefore, fluctuations in the oil market significantly affect gasoline prices. Sometimes, disruptions in the oil market are felt immediately at the pump. Also, refiners are currently operating at near full capacity, suggesting that even if the crude oil supply situation were to ease, refiners would still be hard-pressed to produce more gasoline.⁵⁴ Events such as Hurricane Katrina, which shut down 10 percent of the U.S. refining capacity, only compound the situation. As of February 20, 2006, the national average gasoline price was \$2.24 per gallon. This is \$0.34 more than the gasoline price for the same week in 2005, an increase of 15.2 percent.⁵⁵

While pressures on supply remain, demand also continues to show strong growth. The United States accounts for the largest share of oil demand. Demand in the United States continues to grow, and larger portions of the demand are being met by imports. In the first nine months of 2005, America consumed an average of 20.6 million barrels per day and 60 percent of these barrels were imported.⁵⁶

In 2005, China was the second largest consumer of oil, consuming 6.9 million barrels per day, up from 6.5 million in 2004. Oil demand in China has grown significantly, and continues to surge (see Figure 34). Between 2001 and 2004, China's demand for oil grew 30 percent. In contrast, world oil demand grew 6.2 percent. However, growth in China's demand for oil has slowed in 2005. In the first three quarters of 2005, demand in China was up only 5.4 percent from the first three quarters of 2004. This is compared to an increase of 17.5 percent in 2004. Total world demand was up 1.6 percent in the first three quarters of 2005.⁵⁷

⁵⁴ For more information on current supply and demand conditions in both crude oil production and refining, please see Energy Information Administration, *Short-term Energy Outlook*, <http://www.eia.doe.gov/emeu/steo/pub/contents.html>. (monthly release).

⁵⁵ See Energy Information Administration, *Gasoline and Diesel Fuel Update*, <http://tonto.eia.doe.gov/oog/info/gdu/gasdiesel.asp> (February 2006).

⁵⁶ See Energy Information Administration, *International Petroleum Monthly, Oil Imports*, <http://www.eia.doe.gov/emeu/ipsr/imports.html>, (January 3, 2006).

⁵⁷ Calculations based on oil demand data available from the Energy Information Administration.

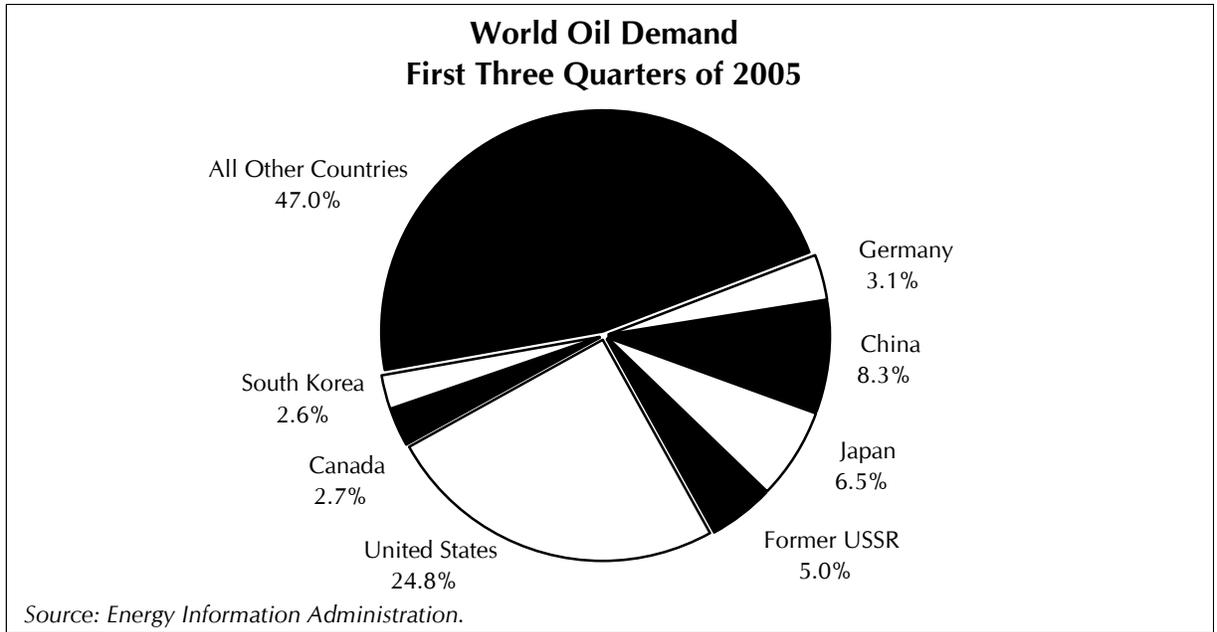


Figure 34

While oil and gasoline may receive the most media attention, natural gas prices represent another significant risk to the energy arena, especially for cold weather areas which require large amounts of natural gas for heating purposes. The monthly Henry Hub spot price (nominal) is higher than it has been in several years (see Figure 35).⁵⁸ Prices are expected to remain high throughout the winter heating season. This will have a significant impact on consumers in the northern United States. Households that heat primarily with natural gas can expect to spend \$178 (or 24 percent) more for fuel this season compared to last winter.⁵⁹

⁵⁸ Henry Hub is a pipeline hub on the Louisiana Gulf Coast and is the delivery point for natural gas futures contracts on NYMEX. The Henry Hub spot price is widely reported in the media when discussing natural gas prices.

⁵⁹ Energy Information Administration, *Short-term Energy Outlook*, <http://www.eia.doe.gov/emeu/steo/pub/contents.html> (February 7, 2006).

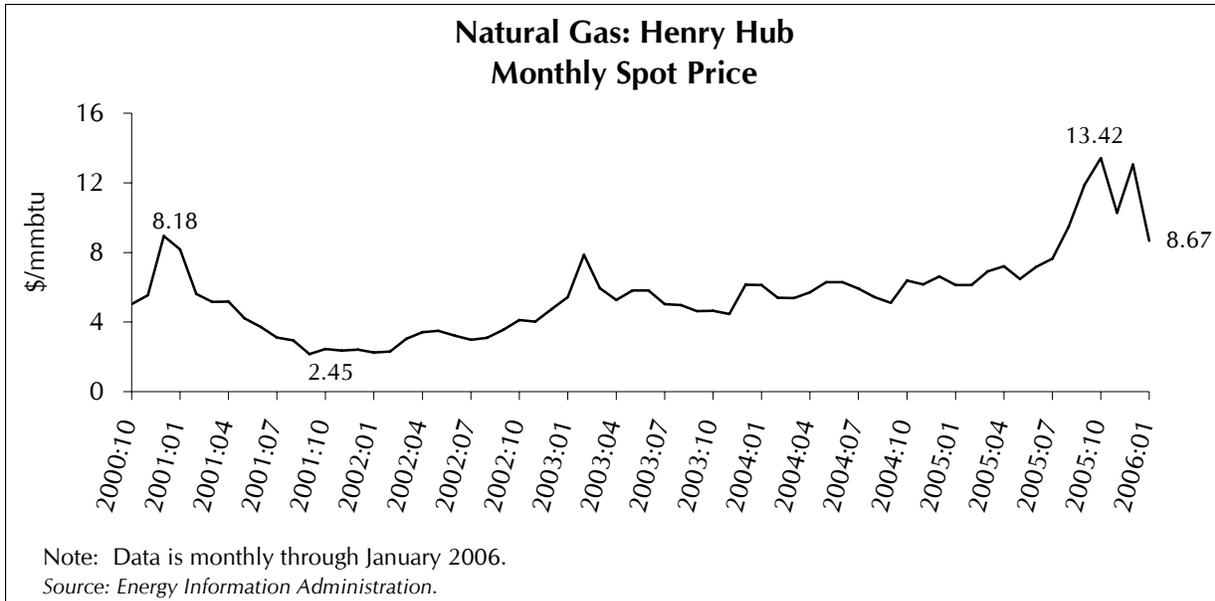


Figure 35

Businesses are also hard hit by high energy prices, especially those in industries that are energy intensive, such as manufacturing. Higher energy prices also can be the breaking point for industries that are already having economic difficulties. For example, the airline industry was severely hurt by the September 11th terrorist attacks. On September 14, 2005, both Delta and Northwest airlines filed bankruptcy. While energy prices were not the sole reason for bankruptcy, both airlines cited high energy prices as the final straw to their already struggling businesses.⁶⁰

Consumer sentiment is also volatile when energy prices change quickly. Consumers react to high gasoline prices or high heating costs, causing a decrease in consumer confidence and consumer sentiment. Although consumer sentiment reacts to higher gasoline prices in a negative way, the effect may be partially offset by other positive factors in the economy, such as strong wage growth and low unemployment. In October 2005 the consumer sentiment index was at its lowest value since October 1992, but it has since rebounded.⁶¹

Consumers have been spending an increasing amount of money on energy expenditures over a long-term period (see Figure 36). As the day to day amount consumers must spend for energy-related products rises, consumers must reduce other purchases, use credit, or dip into savings. Low-income families will be hardest hit by the increases.

⁶⁰ Chris Isidore, "Delta Air Lines Files for Bankruptcy," *CNN Money*, <http://money.cnn.com/2005/09/14/news/fortune500/delta/index.htm?cnn=yes> (September 15, 2005).

⁶¹ "University of Michigan Consumer Sentiment Survey Analysis," Moody's Economy.com, January 2006 (released monthly).

Moody's Economy.com estimates that about half of the increase in energy spending seen after Hurricane Katrina was financed through borrowing.⁶²

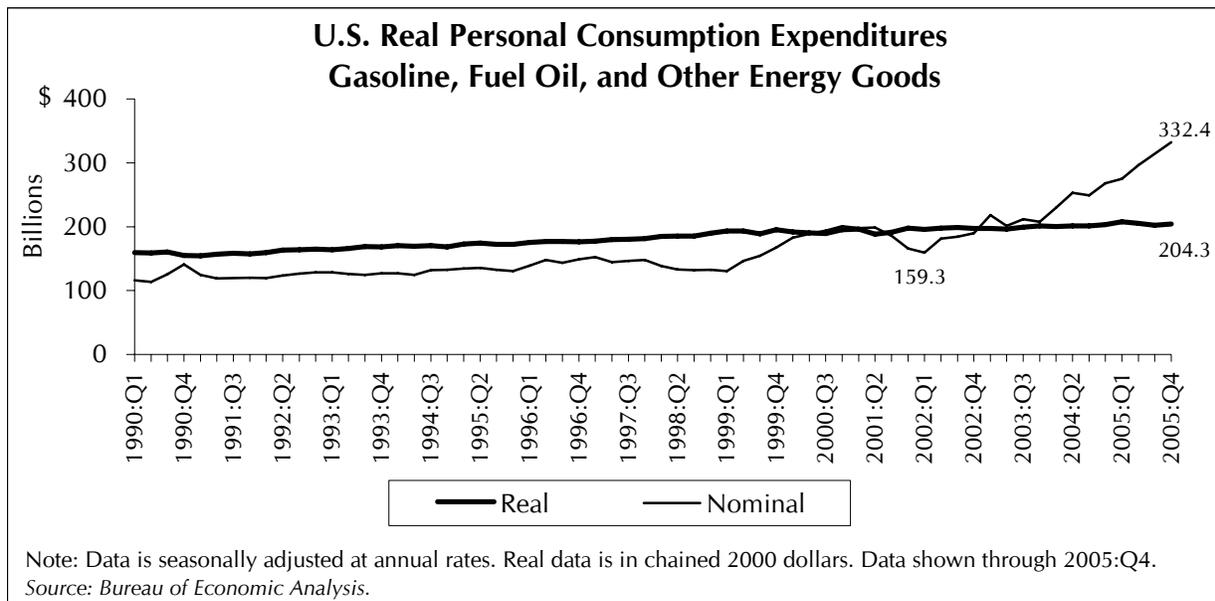


Figure 36

When adjusted for inflation, energy expenditures have followed a slow, steady, upward trend. But the share of real personal consumption expenditures spent on all energy products has decreased since the 1990s from over 3 percent to 2.6 percent.

Corporate Profits

Despite the recent surge in volatility, corporate profits have been improving since 2001 when profits declined 8.5 percent on an accounting basis and 6.2 percent on an economic basis.⁶³ Economic profits increased by 12.6 percent year-over-year during 2004, following a healthy rebound of 16.4 percent in 2003. The large improvement in 2003 and 2004 was due to robust growth in productivity, among other reasons. After growing an estimated 15.9 percent during 2005, economic profit growth will slow to 9.1 percent during 2006 and further down to 5.8 percent during 2007, as output growth is expected to slow and labor and interest costs are expected to rise.

⁶² Comment by Mark Zandi, Chief Economist of Moody's Economy.com, in teleconference on September 7, 2005.

⁶³ Accounting profits (also known as "before-tax profits" in NIPA Table 1.12) are derived from economic profits, which are computed based on net national output. Since net national output is gross national output minus capital depreciation, a decline in capital depreciation, with all other factors held equal, would result in larger net national output and larger economic profits. Two adjustments are made to economic profits to arrive at accounting profits: one is capital depreciation adjustment and the other is inventory valuation adjustment. These adjustments convert capital depreciation and inventory withdrawals from historical cost to replacement cost, which is the measure used in the BEA's national income and product accounts.

Due to robust growth in economic profits, accounting, or before-tax profits, also increased 13.0 percent during 2004, following a healthy year-over-year rebound of 22.0 percent in 2003. As the 50 percent bonus depreciation deduction expired on January 1, 2005, accounting profits surged 126.0 percent on an annualized basis in the first quarter of 2005, resulting in an estimated 34.6 percent year-over-year growth in 2005.⁶⁴ It is forecast to slow to 7.2 percent in 2006 and 5.5 percent in 2007.

Hurricane Katrina destroyed an estimated \$55 billion of physical property (residential structures, business structures and equipment, and proprietors' structures and equipment), causing economic corporate profits for the third quarter of 2005 to plummet by 15.2 percent (at an annualized rate), compared to the second quarter. Capital depreciation usually increases gradually as physical capital stock accumulates over time. But when a large amount of physical property is destroyed during a particular quarter (by disasters such as earthquakes, hurricanes, or terrorist attacks) capital depreciation surges in that quarter, followed by a sizable decline in the next quarter. Since capital depreciation is treated in NIPA as expense that occurs in the process of production, a surge in capital depreciation during a particular quarter results in a big drop in corporate profits on an economic as well as accounting basis in that quarter. As capital depreciation drops in the following quarter, a corresponding big surge in corporate profits follows in the same quarter. So the impact of Katrina on corporate profits would look less severe over the two-quarter period immediately after Katrina hit the U.S. Gulf Coast region.

⁶⁴ The main reason for this recent volatility in before-tax corporate profits was that U.S. corporations were allowed large extra first-year depreciation deductions for qualified equipment, software, and leasehold property. The first-year write-offs were 30 percent more under the provisions in the Job Creation and Worker Assistance Act of 2002. The extra write-offs were raised to 50 percent in the Jobs and Growth Tax Relief Reconciliation Act of 2003. Consequently, corporations wrote-off \$240.2 billion in the first quarter of 2004. As the 50 percent extra depreciation deduction provisions expired on January 1, 2005, however, corporate write-offs declined significantly, pushing up profits reported by corporations in 2005.



Figure 37

With both employment and unit labor cost growing more slowly during the current expansion than previous expansions, robust productivity growth has contributed to the recent strength in corporate profits. As a result, the share of corporate profits in national income has recently risen to around 12 percent from the nine-year low 8.0 percent seen in the third quarter of 2001, while the share of labor income (the sum of wages and salaries and employee benefits) has declined to around 65 percent from the 66.8 percent seen in the same quarter (see Figure 38). As employment recovers, the labor income share may gain in the near future. However, the relatively larger share of corporate profits in national income, seen since the second half of 2003 (except for a couple of quarters), will likely remain intact during the forecast period.

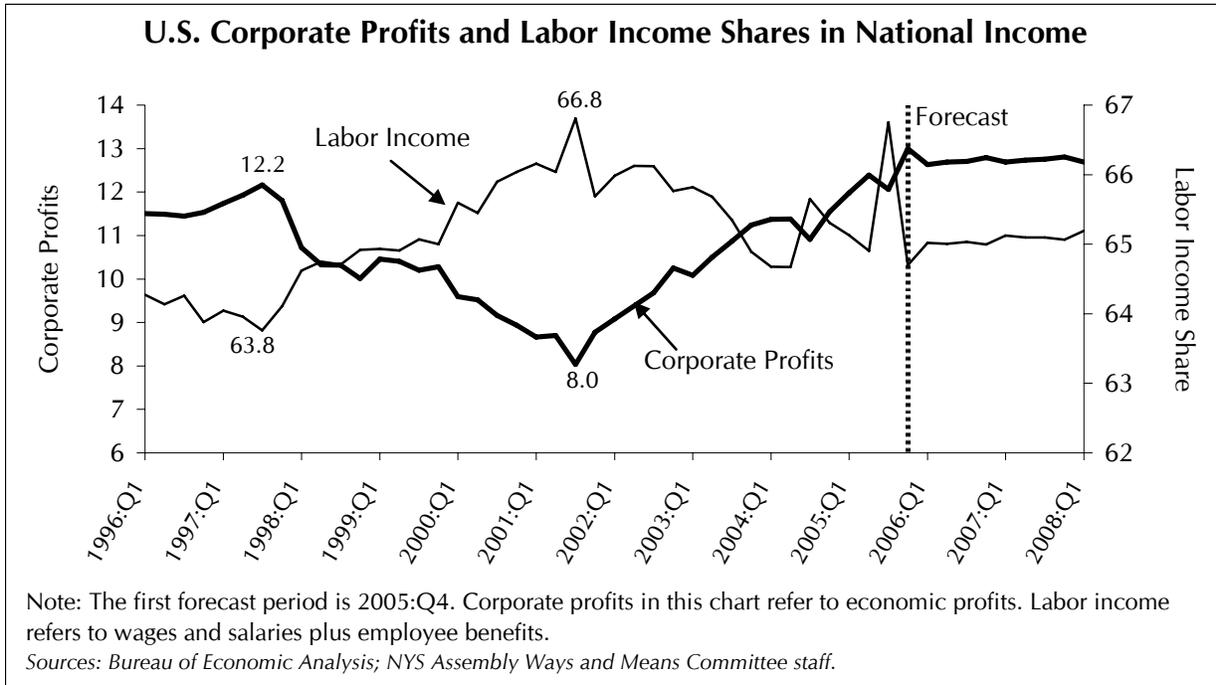


Figure 38

Interest Rates

The federal funds rate averaged 3.2 percent in 2005, 4.7 percent in 2006, and 4.8 percent in 2007. The three-month Treasury bill rate averaged 3.2 percent in 2005, 4.6 percent in 2006, and 4.7 percent in 2007. The ten-year Treasury note rate is forecast to average 4.3 percent in 2005, 5.0 percent in 2006, and 5.3 percent in 2007. The three-month Treasury bill rate by the first quarter of 2008 will be 3.87 percentage points higher than its recent low point of 0.92 percent in the first quarter of 2004, while the 10-year Treasury note rate by the first quarter of 2008 will be 1.68 percentage points higher than its recent low point of 3.62 percent in the fourth quarter of 2003 (see Figure 39).

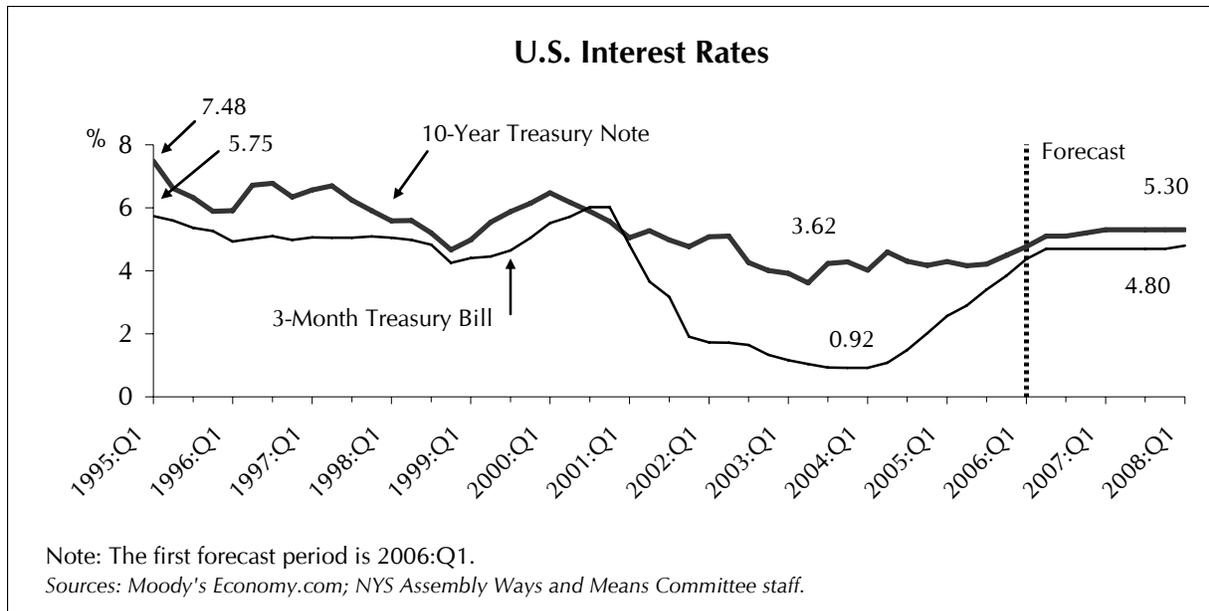


Figure 39

In the period between June 2004 and January 2006, the federal funds rate more than quadrupled, rising from 1.0 percent to 4.5 percent currently. This has been the result of fourteen quarter-point increases implemented by the Federal Reserve. Before the first increase in June 2004, the federal funds rate had remained at an unusually low rate of 1.0 percent for a year. The federal funds rate had not been this low since 1961 using weekly data.

The leadership of the Federal Reserve has changed in February 2006. Although it is expected that any changes in policy will be gradual and that the new chairman will emphasize transparency in Fed activity, any change of this magnitude increases the level of uncertainty regarding interest rates.

In deciding whether to increase the federal funds rate any further, the Federal Reserve must weigh the inflationary pressure (which is reduced by increasing rates) against the risk of a recession or stagnant growth (this risk is reduced by lowering rates). One of the most important recent economic developments has been rapidly rising energy prices, due both to hurricanes and other market factors. Rising energy prices put further pressure in both directions by increasing inflationary pressure while also increasing the risk of a recession. Therefore, the net effect of recent energy price developments may be fairly neutral in terms of expected changes to the federal funds rate.

The behavior of long-term rates over the last two years has been puzzling to many experts. According to one school of thought, the long-term rate is based on future expected short-term rate plus a risk premium. However, the long-term rate has not responded to the dramatic upward movement of the short-term rate. An alternative school of thought holds that the market for short- and long-term bonds is segmented with different types of investors

in each market. This implies that short- and long-term rates do not necessarily move together. The high current account deficit in the United States also has not raised rates, even though this happened in past periods of high current account deficits such as in the first half of the 1980s.

There are a variety of explanations for the low long-term interest rate. Traditionally, low long-term rates despite a high short-term rate have been explained by an expectation of low inflation in the future, or low economic growth. In fact, “inversion” of the yield curve, where the long-term rate is lower than the short-term rate, has historically been a very good predictor of an imminent recession. Some other more recent explanations of the low long-term rate relate to the fact that international financial markets are more interrelated than ever before making the long-term interest rate more responsive to international forces than it is to the Federal Reserve’s actions. Therefore, with rates low internationally, as long as the United States remains a relatively safe investment destination, capital will continue flowing in. In addition, foreigners have been buying United States securities for a variety of reasons. Foreign ownership of these securities has almost doubled in the last decade. Foreign long-term debt ownership has jumped from 11 to 20 percent (see Figure 40) while foreign equity ownership increased from 5 to 9 percent (see Figure 41).

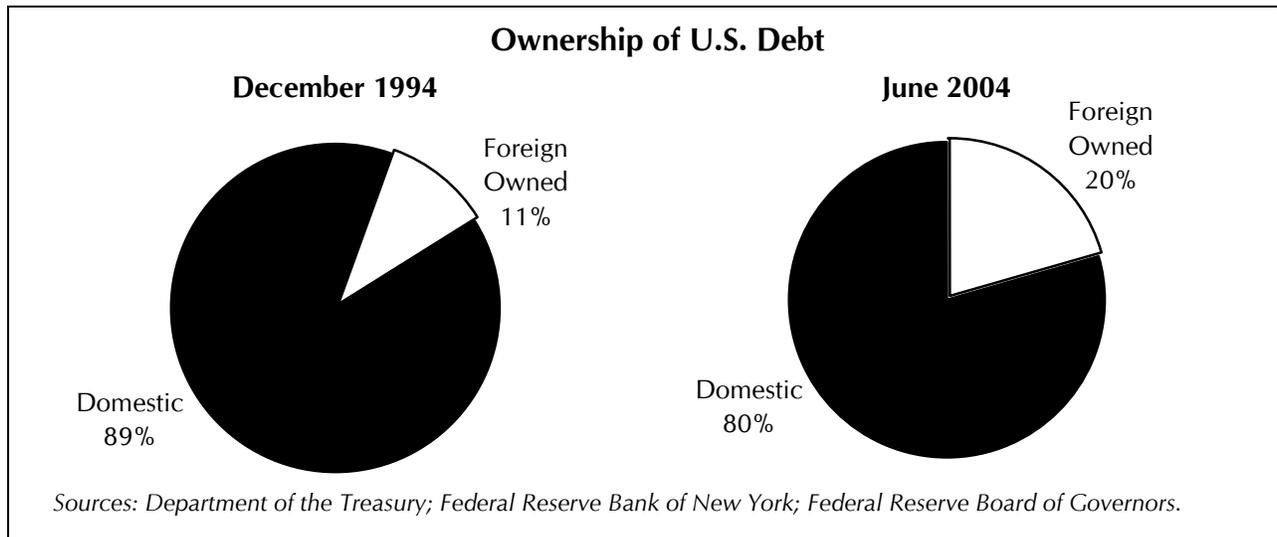


Figure 40

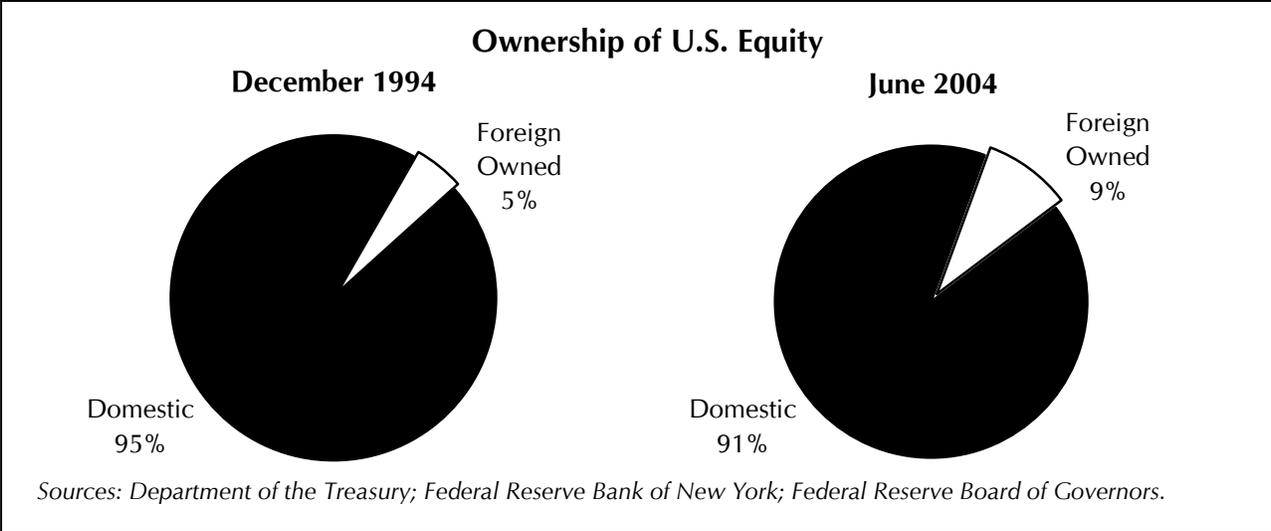


Figure 41

The greatest attention has gone to China which has been buying United States securities to keep the value of its own currencies low. However, the countries that are the largest owners of United States securities are Japan and the United Kingdom (see Figure 42), which have most likely purchased these securities for their investment value rather than to manipulate currency values. Just 7 percent of the long-term United States securities owned by foreigners belong to China. Foreign purchases of United States securities have helped to keep long-term interest rates here low. Another part of the explanation related to international flows is that there may be a collapse in expected profits occurring outside the United States, causing capital to flow into the nation.

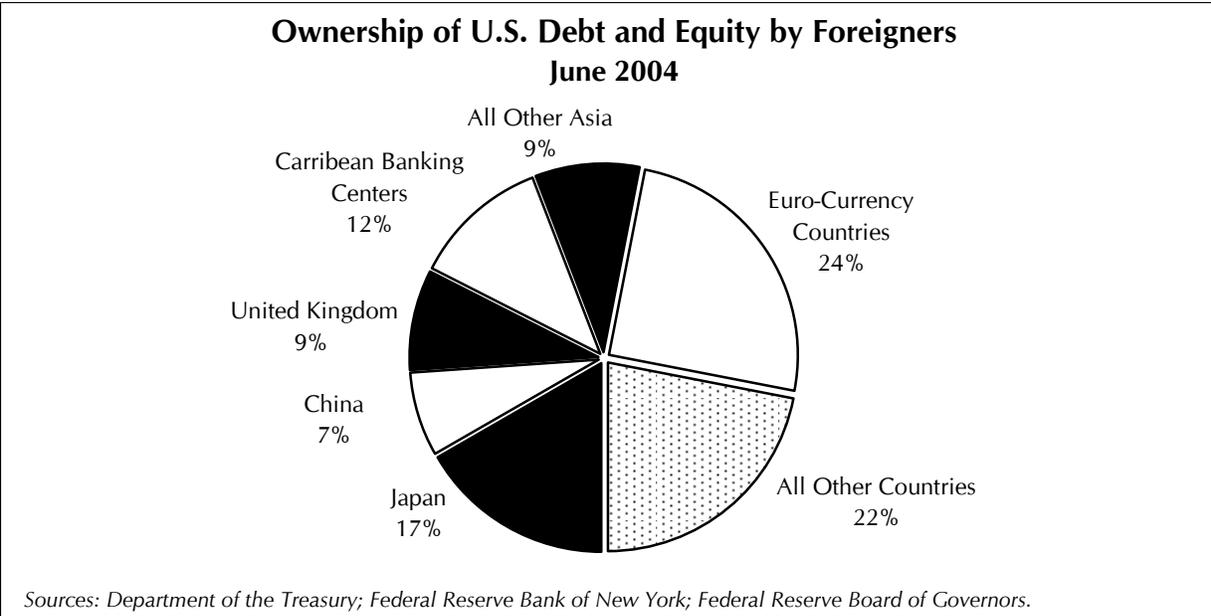


Figure 42

Stock Market

Using yearly average values, the S&P 500 index increased 17.3 percent year-over-year in 2004 following annual declines for three years straight in 2001, 2002, and 2003.⁶⁵ The S&P 500 index grew 6.8 percent year-over-year to 1,207 using yearly average values in 2005. This will be followed by 9.0 percent growth in 2006, and 7.7 percent growth in 2007.

After rising rapidly throughout most of the 1990s and into 2000, stock prices as measured by the S&P 500 index declined sharply from late 2000 until early 2003. The decline took away about half of the stock price gains experienced since 1990. Since the first quarter of 2003, stock prices have generally been rising, although at a very modest pace. The S&P 500 is not expected to return to its former peak of 1,476 reached in the third quarter of 2000 during the forecast period (see Figure 43), although it will come close to this peak by the first quarter of 2008.

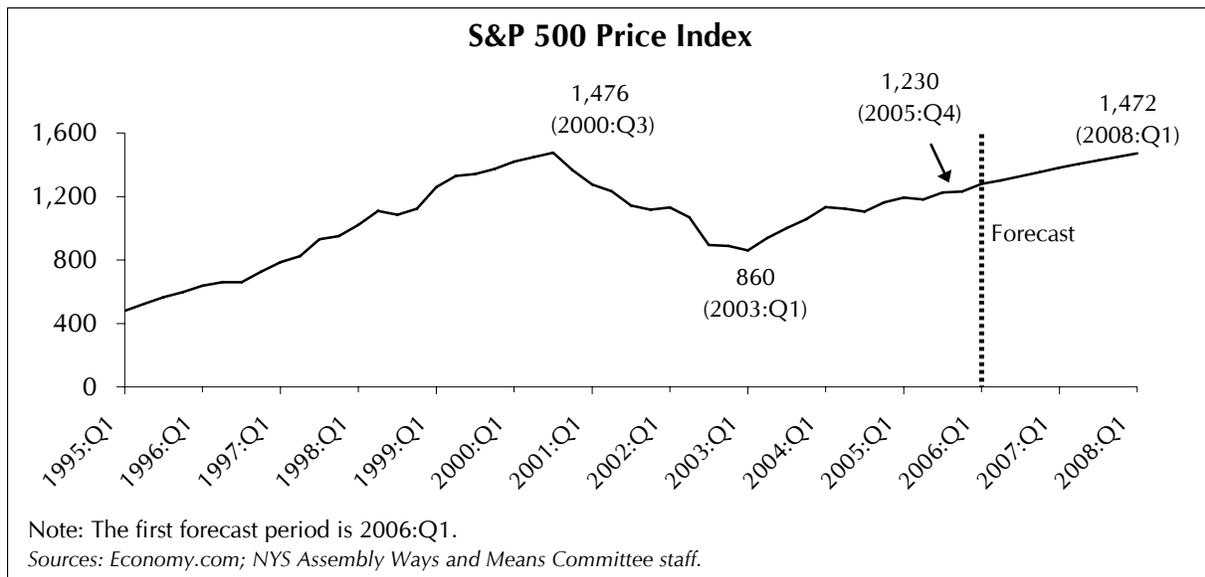


Figure 43

The NASDAQ and Dow Jones Industrial Average (DJIA) have shown trends similar to the S&P 500 (see Figure 44). Based on year-end price, all three markets peaked in 1999 and bottomed out in 2002.⁶⁶ Though the pattern was similar, the NASDAQ had a much more pronounced peak and trough, consistent with the higher volatility of this market which is heavily weighted towards growth and technology stocks. While the S&P 500 and

⁶⁵ This method of comparison is used to be consistent with other growth rates cited in this report. However, yearly growth rates for the stock market are often cited using year-end values rather than yearly averages.

⁶⁶ The 2000 peak in the S&P 500 discussed previously was based on quarterly data. However, since stock prices started declining in the first half of 2000, the annual average price was higher in 1999 than in 2000.

DJIA are well on their way towards their prior peak, the NASDAQ remains at only about half of its peak value.

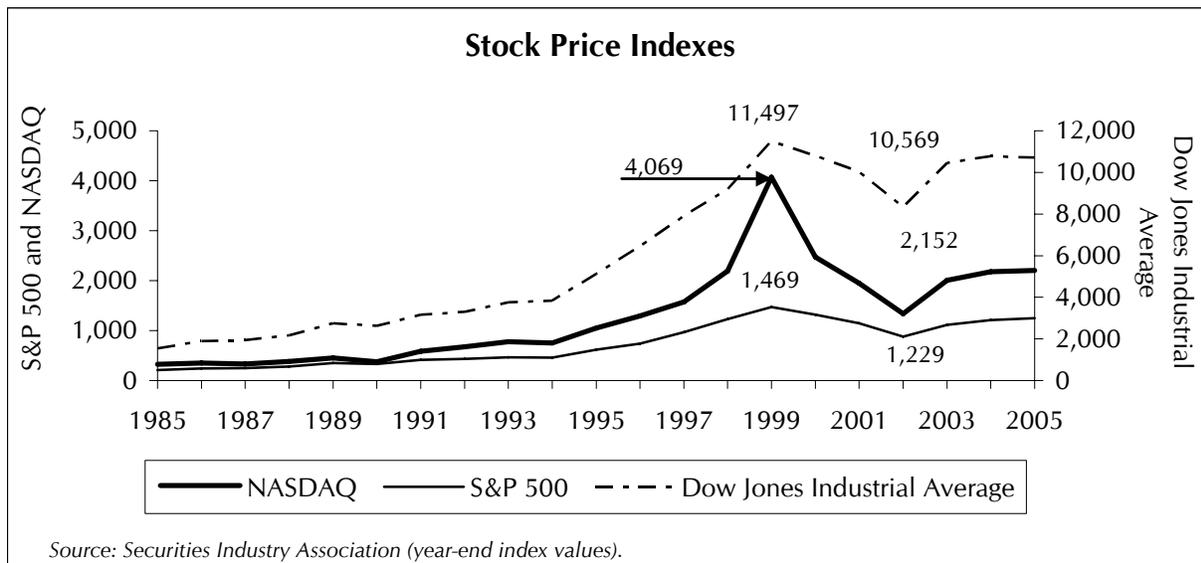


Figure 44

United States Forecast Comparison

The Assembly Ways and Means Committee staff's overall national economic growth forecast is 3.2 percent for 2006 and 3.1 percent in 2007 (see Table 4). The Committee staff forecast for 2006 is 0.1 percentage point lower than Global Insight and Blue Chip. In the February 2006 Blue Chip Consensus forecast, twenty-four out of fifty-three forecasters predicted higher growth in 2006 than the Committee staff.

The Ways and Means Committee staff's overall national economic growth forecast for 2007 is 3.1 percent. It is 0.4 percentage point higher than the Division of the Budget and 0.1 percentage point higher than Moody's Economy.com. It is lower than Macroeconomic Advisers by 0.3 percentage point.

Table 4

U.S. Real GDP Forecast Comparison				
(Percent Change)				
	Actual	Estimate	Forecast	Forecast
	2004	2005	2006	2007
Ways and Means	4.2	3.5	3.2	3.1
Blue Chip Consensus	4.2	3.5	3.3	3.1
Division of the Budget	4.2	3.5	3.2	2.7
Moody's Economy.com	4.2	3.5	3.5	3.0
Macroeconomic Advisers	4.2	3.5	3.5	3.4
Global Insight	4.2	3.5	3.3	2.7

Sources: NYS Assembly Ways and Means Committee staff; Blue Chip, February 2006; NYS Division of the Budget, Executive Budget 2006-07 with 30-day changes, February 2006; Moody's Economy.com, February 2006; Global Insight, February 2006; Macroeconomic Advisers, January 2006.

NEW YORK STATE FORECAST

The New York State economy continues to lag the United States economy in terms of employment growth. However, the State will continue to benefit as the nation maintains an expansion. Wages in New York State are expected to show strong growth in 2006 and 2007. Employment is expected to grow 0.9 percent in both 2006 and 2007, after growing only 1.1 percent in 2005.

New York State employment will grow slower than the national employment in 2006 and 2007. Since the loss of jobs in the 2001 recession was steeper and more prolonged in the State compared to the nation, the recovery will also take longer.

New York will also gain from a positive securities industry outlook. Although industry employment is not expected to return to its 2001 peak during the forecast period, growth in the industry will continue to contribute to State economic growth. Growth in variable compensation will decelerate somewhat throughout the forecast period.

Employment

Figure 45 shows that the rate of decline in employment in New York State during the recent recession was faster than the rate of employment decline in the nation. The percent loss in State employment from the State employment peak to trough was 3.7 percent, compared to 1.9 percent in the United States in the same period. New York State's employment decline started around the same time as the nation, but the rate of decline was much steeper during 2001, due in part to the effects of September 11th. In the employment expansion, New York is expected to create jobs at a slower pace; State employment is expected to grow 4.1 percent between the second quarter of 2003 and the first quarter of 2008, while U.S. employment is expected to grow 6.8 percent. If the New York were to grow at the same rate as the nation in this period, the State would gain an additional 225,400 jobs.

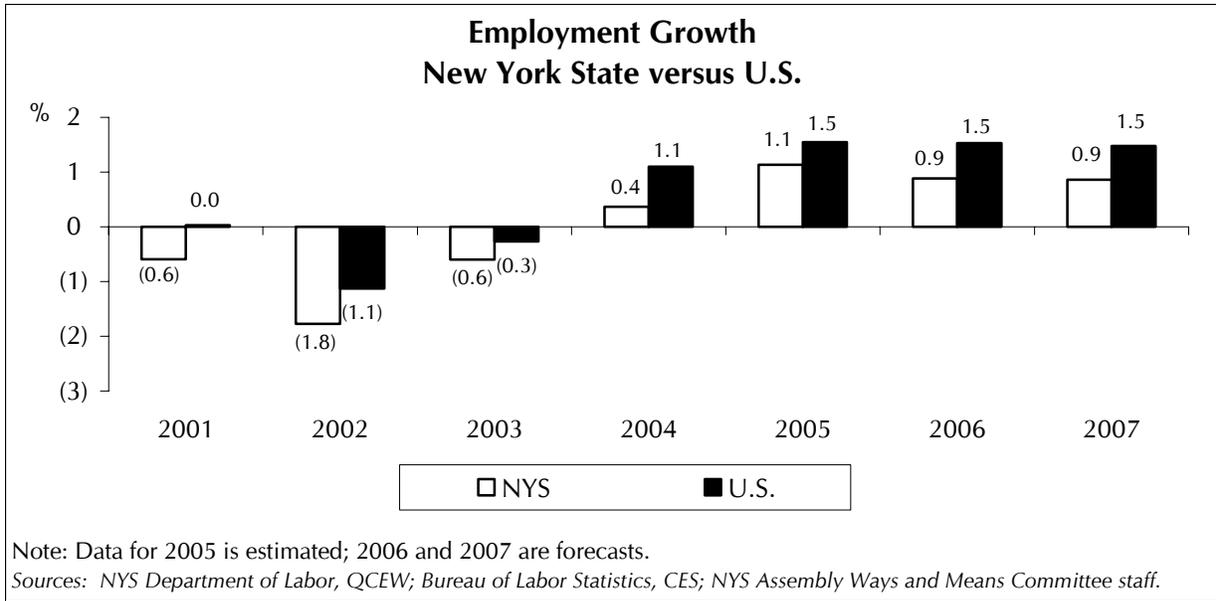


Figure 45

In 2005, New York State accounted for approximately 6.4 percent of total United States employment. This indicates that the State is ranked third in size of employment, behind California and Texas. New York State lags these other large employment states in terms of employment growth, however. New York State employment growth in 2005 was ranked 42nd (see Table 5).

Table 5

2005 Employment Growth and Share of National Employment By State				
Geography	Employment Growth		Share of Total U.S. Employment	
	Growth	Rank	Share	Rank
United States	1.6	-	100.0	-
Nevada	6.3	1	0.9	32
Arizona	4.1	2	1.8	21
Utah	3.7	3	0.9	34
Idaho	3.6	4	0.5	42
Oregon	3.4	5	1.2	28
Florida	3.3	6	5.8	4
Hawaii	2.8	7	0.4	43
Wyoming	2.5	8	0.2	51
Washington	2.4	9	2.1	16
Colorado	2.1	10	1.7	22
New Mexico	2.0	11	0.6	37
Maryland	2.0	12	1.9	20
Delaware	2.0	13	0.3	45
New Hampshire	1.9	14	0.5	40
Montana	1.9	15	0.3	46
Oklahoma	1.8	16	1.1	29
South Dakota	1.7	17	0.3	47
North Dakota	1.7	18	0.3	48
Virginia	1.6	19	2.7	12
Alaska	1.6	20	0.2	49
California	1.6	21	11.1	1
Vermont	1.5	22	0.2	50
Kansas	1.5	23	1.0	31
Alabama	1.5	24	1.4	23
Minnesota	1.4	25	2.0	19
North Carolina	1.4	26	2.9	11
Texas	1.4	27	7.2	2
Nebraska	1.3	28	0.7	36
New Jersey	1.3	29	3.0	9
District Of Columbia	1.3	30	0.5	39
Iowa	1.2	31	1.1	30
Rhode Island	1.2	32	0.4	44
Pennsylvania	1.2	33	4.3	6
Arkansas	1.1	34	0.9	33
Kentucky	1.1	35	1.4	26
Indiana	1.1	36	2.2	14
Connecticut	1.1	37	1.2	27
West Virginia	1.0	38	0.6	38
Missouri	1.0	39	2.0	18
Wisconsin	0.9	40	2.1	15
Georgia	0.9	41	2.9	10
New York	0.9	42	6.4	3
Tennessee	0.9	43	2.0	17
Illinois	0.8	44	4.4	5
Massachusetts	0.7	45	2.4	13
Maine	0.7	46	0.5	41
South Carolina	0.4	47	1.4	25
Ohio	0.3	48	4.1	7
Mississippi	(0.2)	49	0.8	35
Michigan	(0.6)	50	3.3	8
Louisiana	(3.3)	51	1.4	24

Notes: This data may differ from QCEW data usually used by the New York State Assembly Ways and Means Committee, as it is more timely and may be revised, possibly significantly. Rankings are based on two decimal places.
 Source: Bureau of Labor Statistics, CES.

Table 6

		Employment by Sector New York State			
		Actual 2004	Estimate 2005	Forecast 2006	Forecast 2007
Total Employment	Percent Change	0.4	1.1	0.9	0.9
	<i>Level Change</i>	30.3	93.3	73.5	72.2
Government	Percent Change	(1.7)	1.5	0.3	0.3
	<i>Level Change</i>	(23.9)	21.6	4.7	4.0
Education & Health	Percent Change	1.8	1.7	1.7	1.7
	<i>Level Change</i>	24.8	24.6	24.8	24.7
Wholesale Trade	Percent Change	0.6	(0.4)	0.8	0.8
	<i>Level Change</i>	2.3	(1.4)	2.8	2.7
Retail Trade	Percent Change	1.4	1.4	1.2	1.1
	<i>Level Change</i>	11.8	11.7	10.9	10.1
Other Services ¹	Percent Change	1.2	1.5	1.3	1.2
	<i>Level Change</i>	8.6	11.2	9.9	8.8
FIRE ²	Percent Change	0.8	1.6	1.2	1.2
	<i>Level Change</i>	5.4	11.3	8.4	8.4
Manufacturing ³	Percent Change	(2.6)	(2.4)	(2.2)	(2.0)
	<i>Level Change</i>	(16.2)	(14.2)	(12.9)	(11.4)
Leisure & Hospitality	Percent Change	2.7	1.3	1.6	1.6
	<i>Level Change</i>	17.4	8.5	10.4	10.6
Professional Services	Percent Change	1.8	2.4	2.0	1.9
	<i>Level Change</i>	9.0	12.2	10.8	10.1
Construction	Percent Change	1.2	1.3	1.2	0.6
	<i>Level Change</i>	3.7	4.2	3.8	2.0
Information	Percent Change	(2.6)	(0.9)	(0.7)	(0.9)
	<i>Level Change</i>	(7.1)	(2.4)	(1.9)	(2.3)
Transp. & Utilities ⁴	Percent Change	0.4	1.0	1.2	1.2
	<i>Level Change</i>	1.0	2.5	3.1	3.1
Mgmt. of Companies	Percent Change	(0.8)	2.0	1.1	1.0
	<i>Level Change</i>	(1.0)	2.4	1.4	1.2

Note: Level change in employment is in thousands.

¹ Including Administrative, Support, and Waste Management Services.

² Financial Activities including Finance, Insurance, Real Estate, Rental, and Leasing.

³ Including Mining.

⁴ Transportation, Warehousing, and Utilities.

Sources: NYS Department of Labor, QCEW; NYS Assembly Ways and Means Committee staff.

State employment is expected to grow 0.9 percent in 2006 compared to 1.1 percent in 2005 (see Table 6), and total employment is expected to increase by 73,500 jobs in 2006. The education and health sector will create the largest number of jobs in 2006; in this sector employment is expected to grow 1.7 percent, resulting in an increase of 24,800 jobs. The strengthening economic expansion will also result in notable job gains in retail trade, professional services, and leisure and hospitality. Expansion in these sectors reflects

the increased allocation of consumer spending towards these sectors in the expansion; however, these sectors may be sensitive to an increase in oil prices and to changes in consumer confidence. Manufacturing and information sector employment will decline in 2006 and 2007.

The health industry has been an important component of New York State economy in the recent decades. It accounts for a significant share of employment and wages, as well as the economic activity in the State. While most sectors lost jobs during the recent 2001 economic downturn, the health industry continued to gain employment. This persistent employment gain was caused by both the cyclical as well as the structural change in the economy from industrial to service sectors. In contrast to the manufacturing sector, the health industry is the only sector that showed a significant structural gain during the 2001 economic downturn.⁶⁷

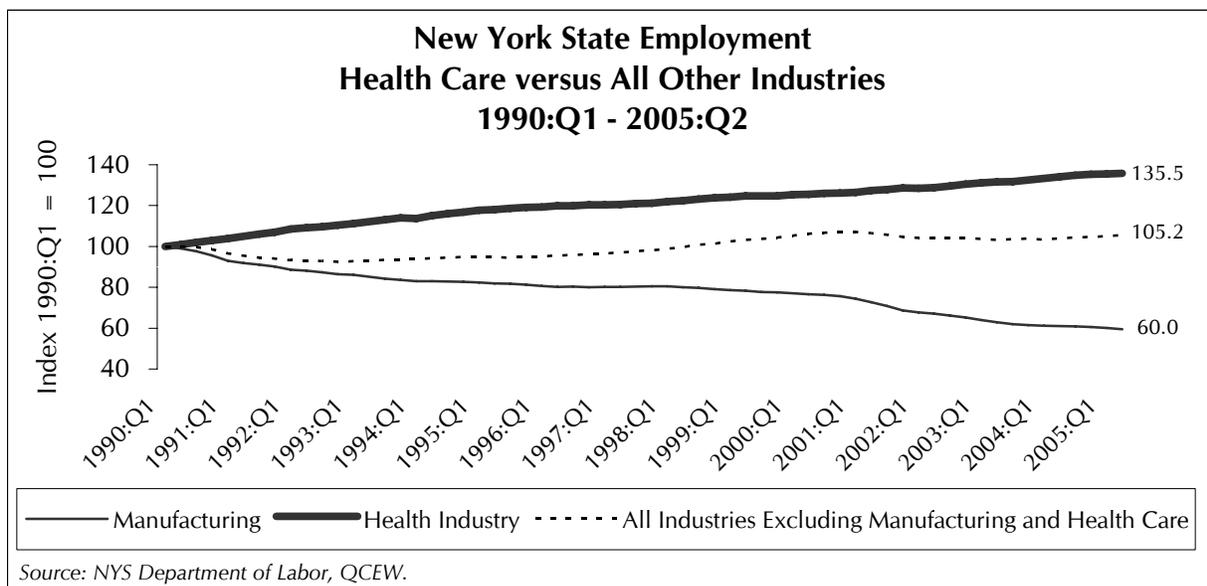


Figure 46

Health employment has been steadily increasing since the 1980s. Health employment rose at roughly a 2.7 percent annual rate between 1983 and 1992, and continued to increase in the recent years, while at the same time total employment in the rest of the economy remained relatively stable (see Figure 46).⁶⁸ From 1994 to 2004, the health industry added 125,300 jobs to New York’s economy, the largest gain among all industries. This has accounted for almost one quarter of the total employment gain in New York State for the same period. Other sectors that experienced similar employment

⁶⁷ Erica L. Groshen, Simon Potter, and Rebecca J. Sela, “Economic Restructuring in New York State,” *Current Issues in Economics and Finance*, 10, no. 7, Federal Reserve Bank of New York, June 2004.

⁶⁸ Ronnie Lowenstein, “The Health Sector’s Role in New York’s Regional Economy,” *Current Issues in Economics and Finance*, 1, no. 5, Federal Reserve Bank of New York, August 1995.

growth to the health industry are other services, leisure and hospitality, and professional services.

Table 7

Employment Change: Recession and Recovery		
New York State		
(Thousands)		
	Employment Downturn	Employment Recovery
	2000:Q4 - 2003:Q2	2003:Q2 - 2008:Q1
Duration (No. of quarters)	10	19
Total Employment	(341.3)	343.4
Education & Health	77.2	119.3
Government	15.1	19.8
Mgmt. of Companies	3.8	5.1
Leisure & Hospitality	(2.4)	56.0
Construction	(14.9)	14.8
Transp. & Utilities ³	(23.5)	12.6
Other Services ¹	(44.6)	47.0
FIRE ²	(53.2)	38.8
Information	(56.8)	(15.2)
Professional Services	(56.8)	50.5
Trade	(59.6)	59.1
Manufacturing ⁴	(125.6)	(64.2)
¹ Including Administrative, Support, and Waste Management Services.		
² Financial Activities including Finance, Insurance, Real Estate, Rental, and Leasing.		
³ Including Mining.		
⁴ Transportation, Warehousing, and Utilities.		
Note: The first forecast period is 2005:Q3. The duration of the recovery period is set at the number of quarters it takes to exceed the employment loss during the downturn. Total Employment is the sum of seasonally adjusted sectoral data.		
Sources: NYS Department of Labor, QCEW; NYS Assembly Ways and Means Committee staff.		

Table 7 gives an indication of the pace of the expected employment recovery in New York State. During the recent economic downturn, 341,300 jobs were lost in the State. These losses were spread over ten quarters between the fourth quarter of 2000 and the second quarter of 2003. It is expected that it will take nineteen quarters for the State to reach the level of employment prior to the employment downturn. By the first quarter of 2008, the employment recovery is expected to generate 343,400 jobs.

The sectoral unevenness in the expansion is evident in Table 7. As in the U.S. employment recovery, job loss in the New York State manufacturing and information sectors is expected to continue as other sectors participate in the employment expansion. Employment growth in the health and education sector and the government sector will

continue in the expansion; in both sectors employment increased during the downturn in the State and the nation.

Table 8 shows the sectoral rates of employment growth in the recent expansion in each region. Employment increased in all regions, though the rates of expansion of the sectors show regional variations. For example, leisure and hospitality employment grew 4.2 percent in the New York City suburbs in the second quarter of 2003 through the second quarter of 2005, whereas the upstate rate of growth in the same sector was only 2.0 percent. Similarly, professional services employment grew 5.6 percent in New York City in the second quarter of 2003 through the second quarter of 2005, while the rate of growth of employment in the same sector in the New York City suburbs was only 0.8 percent. Employment was lost at significant rates in the manufacturing sector and in the information sector in the early stages of the employment expansion in all regions.

Table 8
Employment Change
During the State Employment Expansion
(Percent)

	New York State	New York City	NYC Suburbs	Upstate New York
Total	1.8	2.3	2.2	0.9
Leisure and Hospitality	4.5	6.8	4.2	2.0
Education and Health	3.7	3.1	4.1	4.2
Professional Services	4.1	5.6	0.8	3.9
Retail Trade	3.0	5.3	1.8	2.0
Other Services ¹	3.2	2.4	5.8	1.9
Construction	2.7	0.1	4.5	4.0
FIRE ²	2.4	2.5	2.5	2.1
Transportation and Utilities ³	1.6	(0.1)	4.3	2.0
Government	0.9	2.4	0.3	(0.2)
Wholesale Trade	(0.1)	0.1	(0.4)	(0.1)
Mgmt. of Companies	0.9	(4.4)	10.5	2.4
Information	(3.4)	(1.6)	(4.3)	(7.5)
Manufacturing ⁴	(5.3)	(10.4)	(2.7)	(4.5)

Note: Employment change is for the 2003:Q2 to 2005:Q2 period. Bolded numbers are largest in each sector. State data are the sum of seasonally adjusted regional data.

¹ Including Administrative, Support, and Waste Management Services.

² FIRE includes Finance, Insurance, Real Estate, Rental, and Leasing.

³ Transportation, Warehousing, and Utilities.

⁴ Including Mining.

Source: NYS Department of Labor, QCEW.

The largest regional job gain was in New York City, but there were notable job gains in the New York City suburbs and in upstate New York. In all regions, the largest source of employment level increase was education and health. In this sector, the rate of

job growth was not affected by the economic downturn. During the downturn from the fourth quarter of 2000 to the second quarter of 2003, State education and health employment expanded at the annualized rate of 2.3 percent statewide. During the comparison from the second quarter of 2003 to the second quarter of 2005, the annualized rate of employment expansion was 1.8 percent.

Manufacturing Sector

Between 1994 and 2004, manufacturing employment fell by 226,100 in New York State, reflecting an average annual rate of decline of 3.0 percent (see Figure 47). In the same period, the nation lost 2.8 million manufacturing jobs, which reflects an average annual rate of decline of 1.7 percent. The tendency for manufacturing jobs to decline in both the State and the nation is a feature of more recent decades: in previous decades, national manufacturing employment had increased while State manufacturing employment declined.

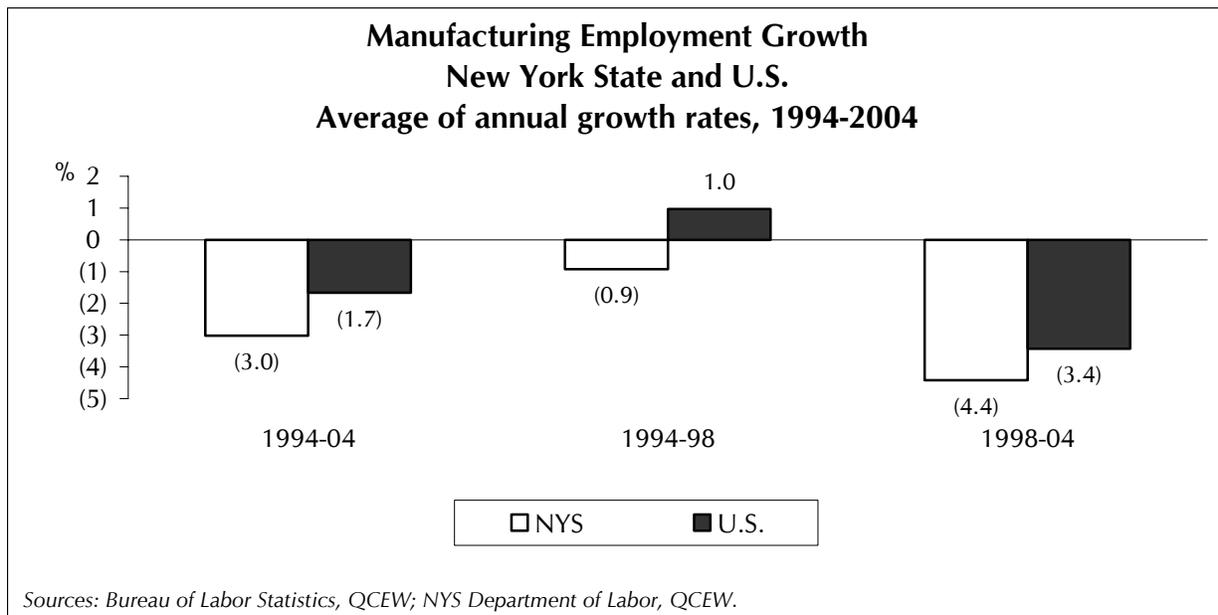


Figure 47

The rate of decline in manufacturing employment increased after 1998.⁶⁹ The decline in U.S. manufacturing employment started in 1998 while New York State manufacturing employment declined throughout the 1994-04 period. This indicates the long-run nature of the decline in the State’s manufacturing employment. The sharp and large rate of decline in U.S. manufacturing employment and the extended duration of this decline indicate that structural factors were involved in the U.S. manufacturing

⁶⁹ U.S. Congress, Congressional Budget Office, *What Accounts for the Decline in Manufacturing Employment*, Economic and Budget Issue Brief, February 18, 2004; Robert E. Hall, “Understanding the Evolution of U.S. Manufacturing,” (testimony before the U.S. Senate Finance Committee, July 8, 2003).

employment decline. These factors include the use of labor saving technologies in production, the deterioration of the U.S. trade balance, and the increase in employee benefit costs. The cyclical decline in the demand for manufacturing goods also contributed to the decline in manufacturing employment: this is seen in the decline in employment in sectors such as computers and electronics, electrical equipment, and machinery. Part of the decline in demand for these goods may also have been on account of the excessive build up in business assets in the expansion of the 1990s.

In 2005, the estimated rate of manufacturing job loss was lower than in preceding years in both the State and the nation. However, the rate of manufacturing job loss in the nation was much lower than in New York State in 2005. In the forecast period, national manufacturing employment is expected to stabilize with virtually no growth, but job losses are expected to continue in the State. Though some of the structural and cyclical job losses were similar in the State and the nation, in New York the structural job losses will be much larger than the cyclical gains in the economic expansion of the next few years due to continued decline in manufacturing industries in New York State relative to the nation.

Securities Industry

Securities industry employment in New York is estimated to have grown 3.9 percent in 2005. It is forecast to grow 3.2 percent in 2006, and 3.4 percent in 2007. This follows a sharp decline during 2002 and 2003 and a return to positive growth in 2004 (see Figure 48). Growth for the industry turned positive in the first quarter of 2004 and is expected to remain strong for the entire forecast period. However, 2007 employment will still be only 94.9 percent of its 2001 peak. Securities industry employment will grow slightly slower in the nation than in New York State, averaging 2.3 percent in 2005, 2.9 percent in 2006, and 3.3 percent in 2007.

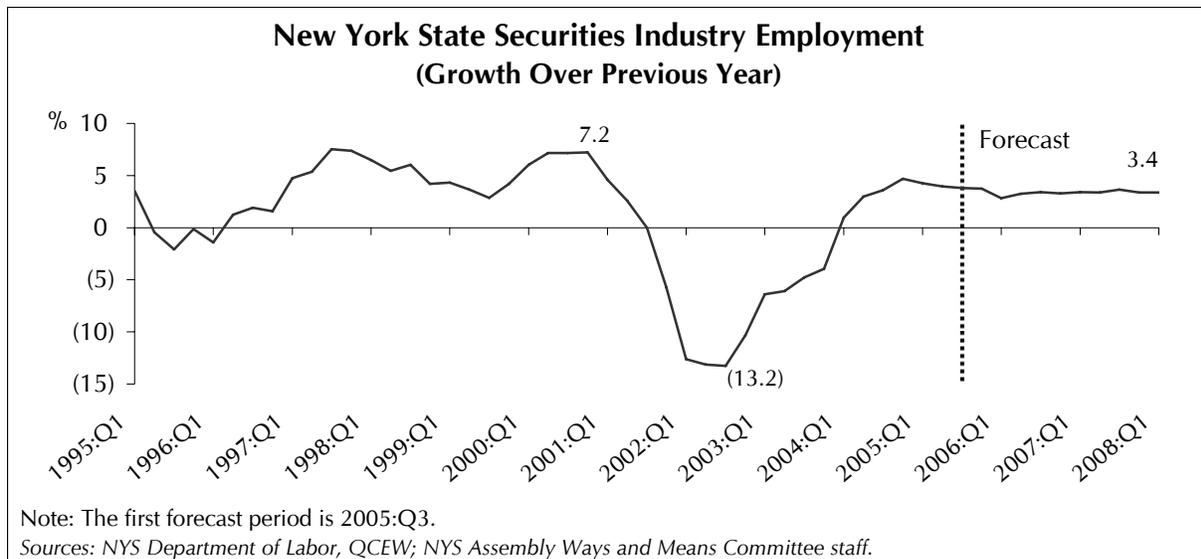


Figure 48

The securities industry is far below its peak profitability in 2001 and even below the profitability levels experienced in 2003 (see Figure 59 on page 72). Some growth in industry profits are expected in the forecast period, however profits will not return to their 2001 peak. Revenue is expected to grow more rapidly than profits. This is mainly due to rising interest rates. Interest revenue and expenses make up a large component of both costs and income for the industry. On balance, the effect of a change in the interest rate is fairly neutral for the industry in terms of the interest revenues minus expenses. Therefore, if interest rates rise as expected in the forecast, both revenue and expenses should rise for the securities industry.

Changes in interest rates can separately have an effect on the industry through trading gains or losses. The securities industry is increasingly taking its own positions in the market through proprietary trading. Large changes in interest rates can cause significant variability in the value of the financial assets held by securities firms. Whether the industry gains additional income from these financial assets or suffers a loss depends on how they bet the market would move relative to what actually occurred. Recently, long-term interest rates have been increasing less than expected by most market analysts (see the Interest Rates section on page 46). This could either have a positive or negative impact on securities industry firms depending on market positions taken. It is also unknown whether this will continue or whether long-term interest rates will now start to increase as predicted in this forecast.

Currently, 21 percent of industry revenue comes from commissions and trading gains, activities related mostly to the trading of stocks and bonds (see Figure 49). Eight percent of revenue comes from underwriting, including initial public offerings, while 7 percent comes from asset management fees. Over half of revenue comes from other revenue sources. The two largest sources of revenue in this category are mergers and acquisitions (M&A) and interest revenue (aside from margin interest). Unfortunately, the current system of categorizing financial data used by the securities industry does not allow revenue from these two categories to be measured precisely.

Probably the strongest area of growth in the securities industry has been in the M&A area which exceeded \$1 trillion in activity for 2005. However, this is still far short of the peak levels before the collapse of the stock market around the time of the 2001 recession. M&A activity will probably continue to be strong, while still not setting new records. Most other revenue areas such as commissions, trading gains, underwriting, mutual fund sales, and asset management fees are expected to be fairly flat or grow slightly during the forecast period.

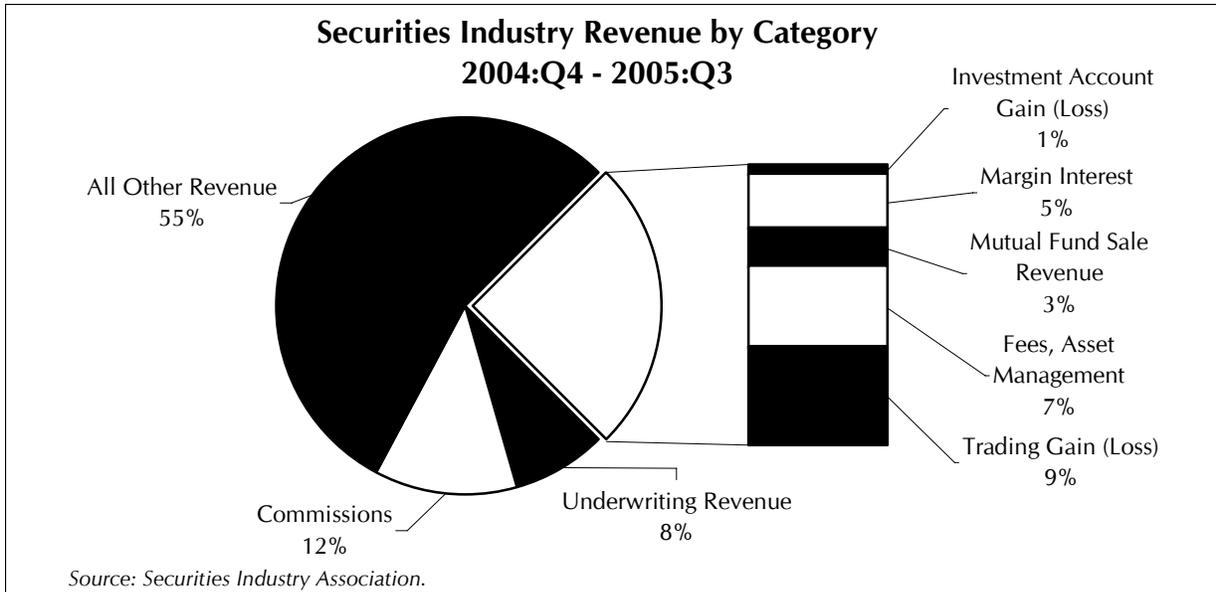


Figure 49

The two greatest expenses for the industry are interest expense followed by compensation (see Figure 50). If interest expenses are not included (because it is mostly offset by interest-related revenue) then most of the expenses of the securities industry are from compensation. Despite a very high presence in expensive high-end Manhattan real estate, less than three percent of the industry's expenses are related to the cost of property (i.e. occupancy expense). Given the structure of these expenses, it is likely that the securities industry will continue to maintain a heavy presence in Manhattan as long as it allows the industry's highly-paid workers to conduct business more efficiently or is simply a more attractive place to work for high-productivity employees.

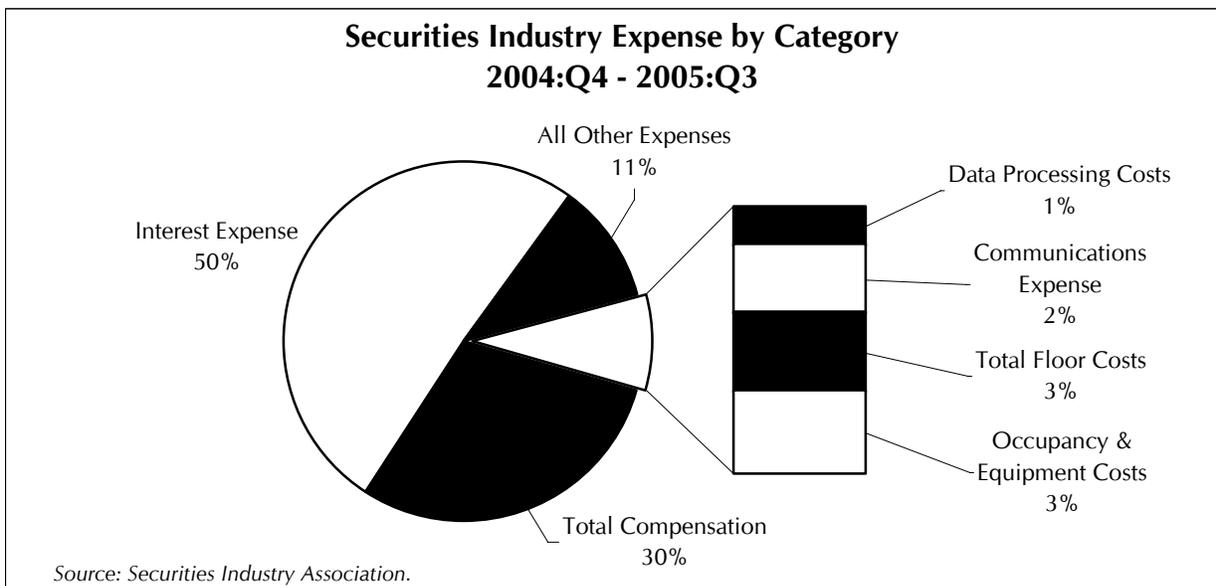


Figure 50

Wages

Wage growth in New York State has not again reached the high levels seen in 2000; however, they are expected to show strong growth in 2006 and 2007. Wages grew 5.3 percent in 2005. The Ways and Means Committee staff predicts State total wages, which are the sum of base and variable wages, will grow 6.1 percent in 2006 and 5.0 percent in 2007.

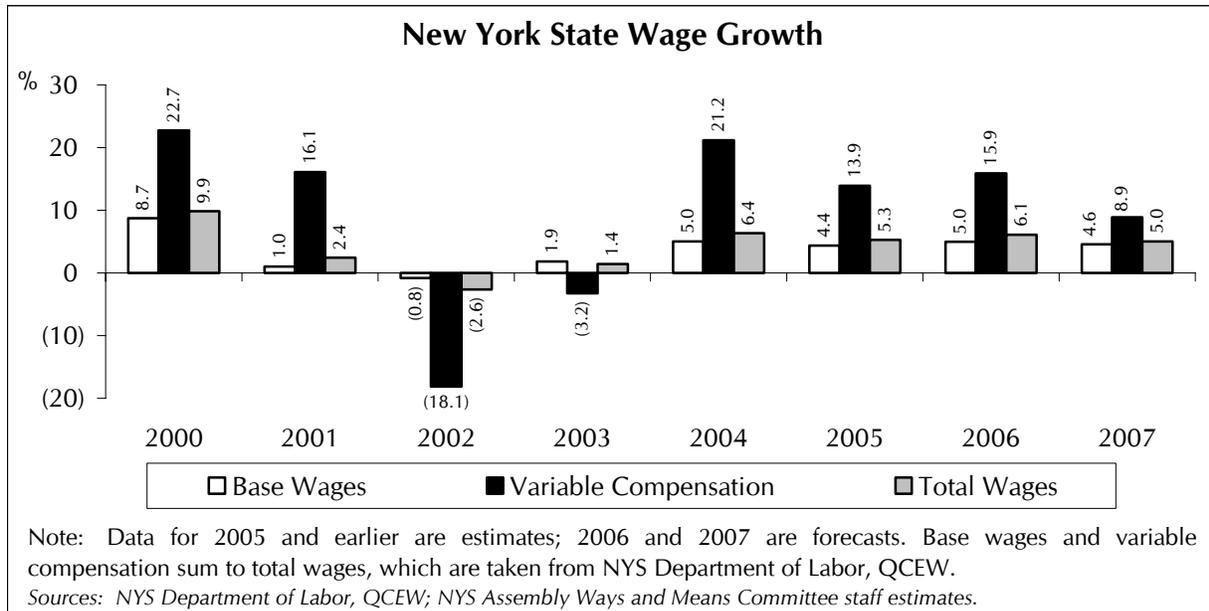


Figure 51

Although wage growth in New York State has not reached the high rates seen in 2000, it has rebounded from a low of negative 7.0 percent in the first quarter of 2002 (see Figure 52). Fueled by a surge in variable compensation wages in the securities industry, wage growth was particularly strong in the first quarter of 2004, reaching 7.9 percent compared to the same quarter a year ago. Base wages and variable wages are expected to continue to grow steadily in 2005 and 2006 and the Ways and Means Committee staff estimates that State total quarterly wages will grow at an annual rate of between 4.5 and 8.7 percent in 2006 and 2007.

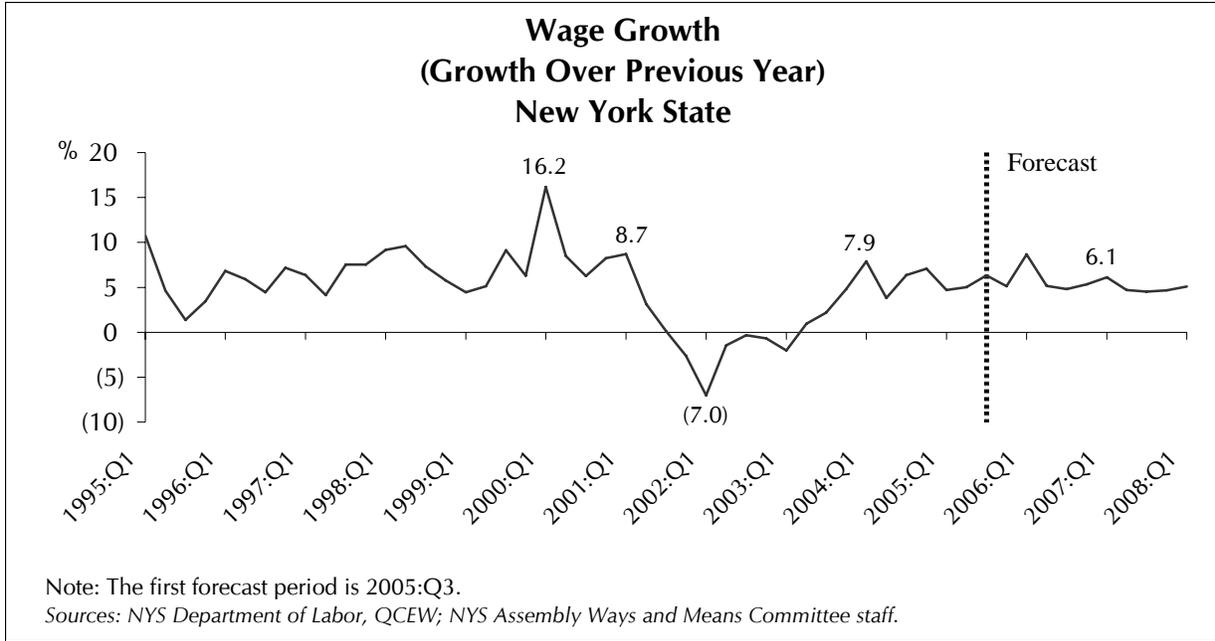


Figure 52

Wage growth in New York State was faster than wage growth in the nation in 2004 (see Figure 53). The strong growth was a result of large increases in variable compensation. Variable compensation growth slowed in 2005, but it is expected to grow 15.9 percent in 2006 and 8.9 percent in 2007.

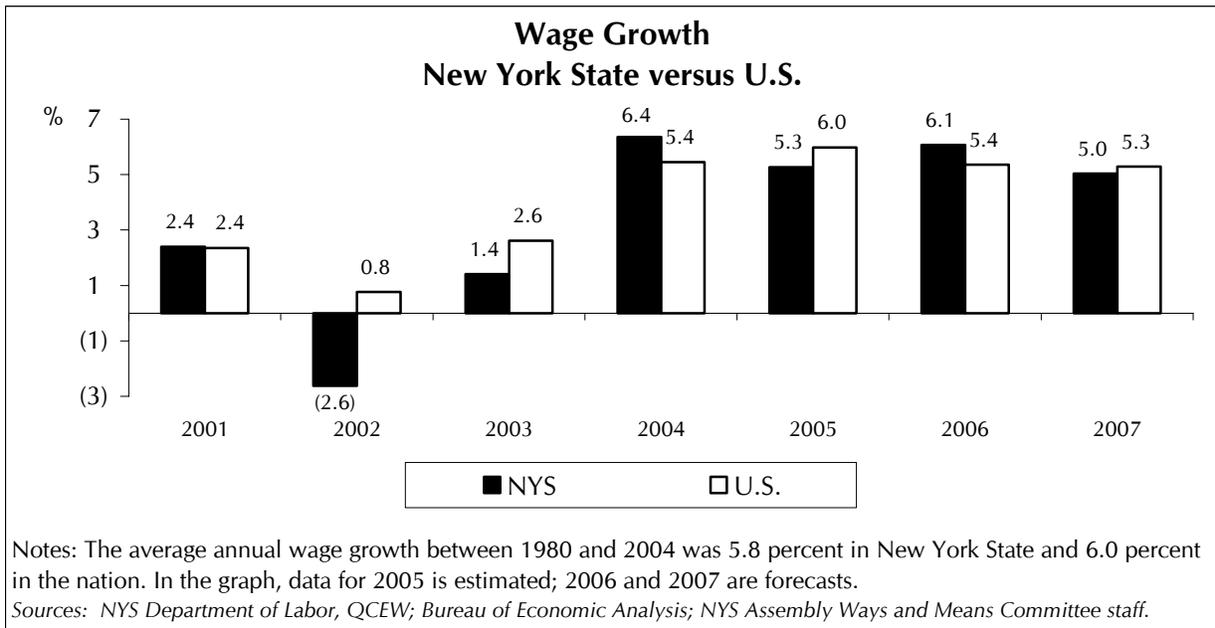


Figure 53

While wages in New York have shown strong growth recently, this growth has not been shared evenly across sectors in the economy (see Table 9). For example, while total wages rebounded in 2003 after declining 2.6 percent in 2002, four sectors did not show wage growth until 2004: Finance, insurance, and real estate (FIRE), manufacturing, information, and management of companies. However, since 1990 FIRE wages have outpaced other industry wages in the State (see Figure 54).

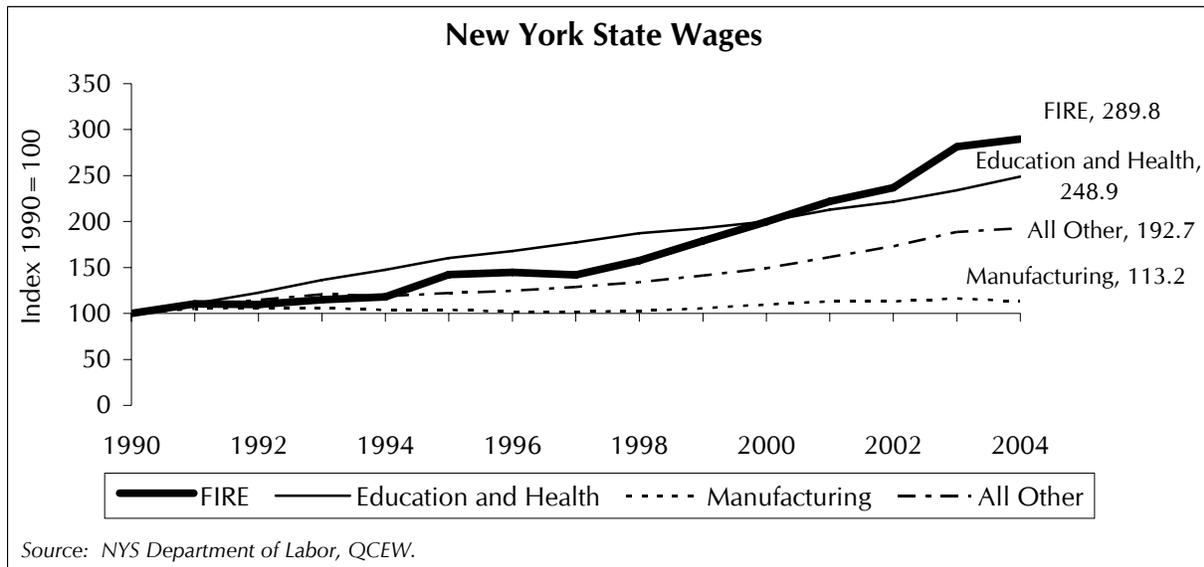


Figure 54

The industries that make up the service-providing sector are currently leading the way in State wage growth. In 2004, the best performing sectors included the FIRE sector (led by growth in the securities industry), professional services, leisure and hospitality (which has shown positive wage growth for the past five years), and management of companies. In terms of total growth, the service sectors are forecast to continue to grow faster than goods-producing sectors throughout the forecast period.

In terms of variable wages, the FIRE sector routinely shows the strongest growth among all sectors in the State. As variable wages are particularly volatile in this sector, this sector also tends to detract greatly from total variable wages when the industry has a poor year.

While the FIRE sector is an important contributor to wage growth in New York State, it also comprises a large share of total State wages, 20 percent in 2004. Other sectors with large shares include government with 15.8 percent, health and education with 12.9 percent, and trade with 10.7 percent. Manufacturing once made up a large portion of State wages (20.4 percent in 1978), but this share has since dwindled to 7.3 percent in 2004. FIRE has gained the largest share since 1978, followed by health and education. The gain in the FIRE sectors share of wages since 1978 (10.5 percentage points) is much larger than the sectors' gain in employment share (0.2 percentage point).

Table 9

**Personal Income, CPI, and Wages By Sector
New York State**

		Actual	Estimate	Forecast	Forecast
		2004	2005	2006	2007
Personal Income	Percent Change	6.9	5.3	6.0	5.5
	<i>Level Change</i>	46.4	37.8	45.7	44.1
CPI	Percent Change	3.5	3.9	3.7	3.0
Total Wages	Percent Change	6.4	5.3	6.1	5.0
	<i>Level Change</i>	24.7	21.7	26.4	23.2
Government	Percent Change	3.9	2.0	3.7	3.7
	<i>Level Change</i>	2.4	1.3	2.5	2.5
Education & Health	Percent Change	6.0	5.5	6.6	6.2
	<i>Level Change</i>	3.0	2.9	3.7	3.7
Wholesale Trade	Percent Change	5.1	4.5	4.5	4.3
	<i>Level Change</i>	1.0	1.0	1.0	1.0
Retail Trade	Percent Change	4.6	3.9	4.1	3.8
	<i>Level Change</i>	1.0	0.9	1.0	0.9
Other Services ¹	Percent Change	5.4	7.1	6.2	5.4
	<i>Level Change</i>	1.2	1.6	1.5	1.4
FIRE ²	Percent Change	14.9	8.8	10.3	7.5
	<i>Level Change</i>	10.7	7.3	9.3	7.4
Manufacturing ³	Percent Change	1.1	1.7	2.0	1.3
	<i>Level Change</i>	0.3	0.5	0.6	0.4
Leisure & Hospitality	Percent Change	6.6	3.1	4.8	4.7
	<i>Level Change</i>	0.9	0.5	0.7	0.8
Professional Services	Percent Change	6.7	8.2	7.1	5.9
	<i>Level Change</i>	2.4	3.1	2.9	2.6
Construction	Percent Change	2.1	3.7	3.8	2.9
	<i>Level Change</i>	0.3	0.6	0.6	0.5
Information	Percent Change	1.9	3.8	3.2	2.6
	<i>Level Change</i>	0.4	0.8	0.7	0.5
Transp. & Utilities ⁴	Percent Change	2.9	3.7	4.5	4.1
	<i>Level Change</i>	0.3	0.4	0.5	0.5
Mgmt. of Companies	Percent Change	6.6	4.8	9.1	5.7
	<i>Level Change</i>	0.9	0.7	1.3	0.9

Note: Level changes in income and wages are in billions of dollars.

¹ Including Administrative, Support, and Waste Management Services.

² Financial Activities including Finance, Insurance, Real Estate, Rental, and Leasing.

³ Including Mining.

⁴ Transportation, Warehousing, and Utilities.

Sources: Bureau of Economic Analysis; NYS Department of Labor, QCEW; Bureau of Labor Statistics; NYS Assembly Ways and Means Committee staff.

Non-variable or base wages show much less volatile growth rates than variable wages. With the employment growth expected throughout the forecast period, base wages can be expected to continue on a path of solid growth. Inflationary pressures may also add to wage gains.

The forecasted wage growth may not be uniform across sectors. For example, in 2004, base wages in the manufacturing sector grew only 1.0 percent while base wages in the FIRE sector grew 10.6 percent. Most other sectors experienced base wage growth of around 3 to 4 percent.

While total wages are volatile because they include variable compensation, base wages generally exhibit a more stable pattern. Base wage growth has been helped by growth in employment as well as average base wages (see Figure 55). Since 2003, base wages have grown faster than the consumer price index in New York State, indicating that real wages have increased. This trend is predicted to continue throughout the forecast period.

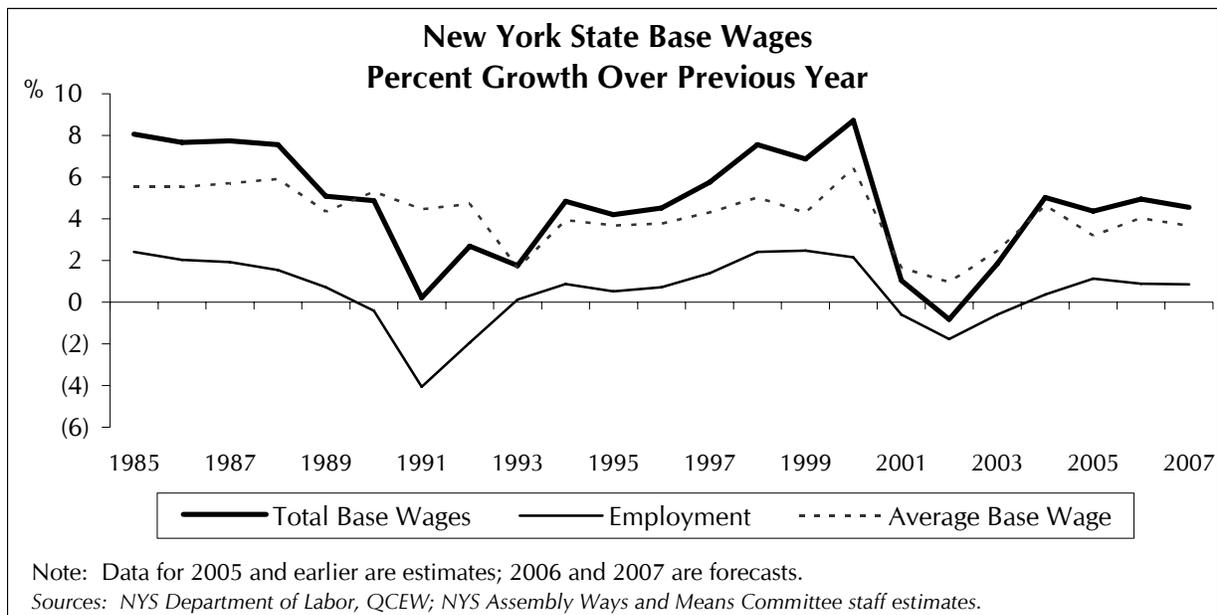


Figure 55

Average wage growth in New York State has kept pace with the growth in United States average wages. The level of the total average wage in New York State is higher than the total average wage in the United States. This is likely due to the State's concentration of the securities industry, which has a much higher and more volatile average wage than other sectors in the State. For example, the average wage in the securities industry in 2004 was \$256,300; in manufacturing, it was \$50,200.

Variable Compensation

Variable compensation is the most volatile component of State wages and plays an important role in forecasting State wages.⁷⁰ Variable compensation has made up 9.2 percent of total compensation over the last five years. However, due to the volatility of this portion of compensation, its importance for forecasting wages is greater than its proportion of wages. The variable component of compensation is particularly prominent in the securities industry. Securities industry variable compensation has made up 46.0 percent of total variable compensation in the State over the last five years.

The second largest source of variable compensation outside of the securities industry is non-securities FIRE. This is followed by professional services, management, and education and health (see Figure 56). Combined, these sectors (i.e. professional services, management, education and health, securities industry, and FIRE) make up over three-quarters of variable compensation. FIRE variable compensation alone, which includes both non-securities FIRE and securities industry) is 59 percent of all variable compensation.

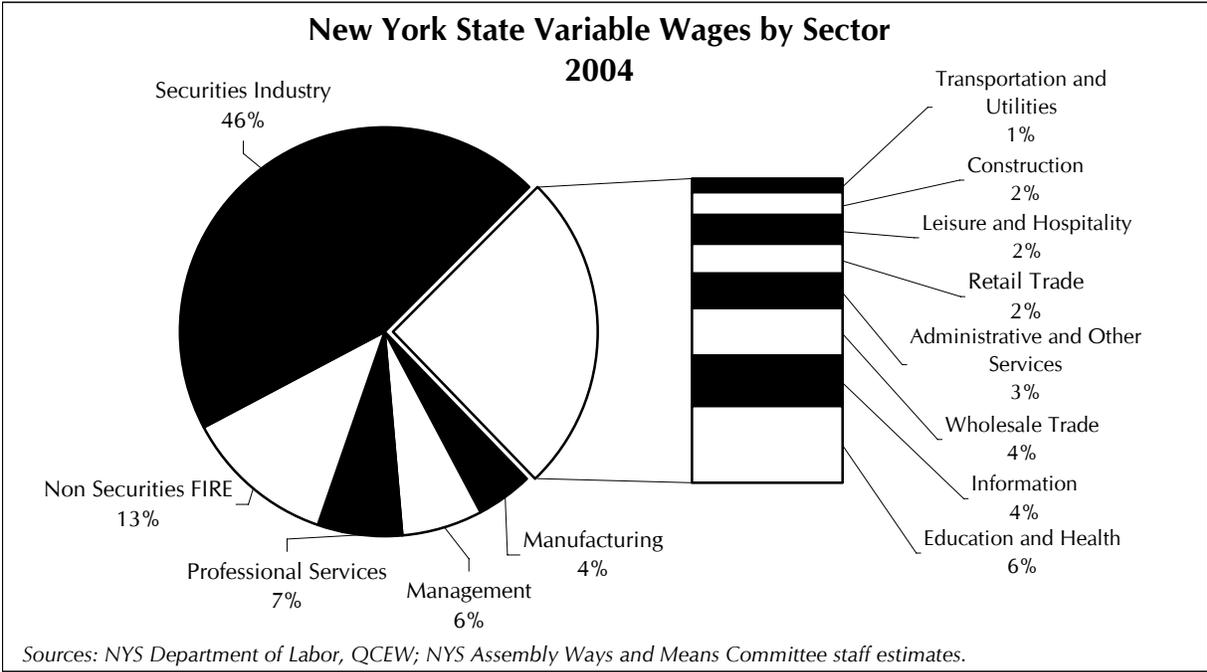


Figure 56

⁷⁰ There is no known series of data for state or national variable compensation. The NYS Assembly Ways and Means Committee staff estimates variable compensation based on seasonal variations in wage patterns. These seasonal patterns are broken down by sector (at the NAICS three-digit level) to improve the precision of the estimate. The growth in this variation over time is also accounted for in the estimate. Since this estimate is based on seasonal variation, it may underestimate bonuses and commissions that come at frequent intervals throughout the year. It also may underestimate stock options to the extent that they are exercised throughout the year. On the other hand, in some cases non-variable pay may be included in variable compensation if there are regular seasonal patterns (such as if overtime regularly occurs in a certain quarter). Therefore, variable compensation contains high uncertainty—even in terms of the data history.

In 2004, variable wages grew in all sectors except for construction and transportation and utilities (see Table 10). These two sectors also happen to be the smallest in terms of variable wages. The largest percentage gains were seen in securities and other services.

Table 10

New York State Variable Wage Change (Percent Change over Previous Year)					
	2000	2001	2002	2003	2004
Total	22.7	16.1	(18.1)	(3.2)	21.2
Securities	72.2	18.4	(28.5)	(11.1)	36.1
Nonsecurities FIRE	(1.6)	15.5	(5.6)	(1.8)	5.1
Professional Services	0.6	(0.8)	(5.3)	(4.0)	25.3
Mgmt. of Companies	68.4	29.2	(4.0)	(8.7)	14.7
Education & Health	(38.5)	18.2	8.6	24.5	7.7
Manufacturing	(0.5)	16.5	(13.7)	(2.0)	2.2
Information	40.3	16.1	(33.8)	6.2	18.9
Wholesale Trade	1.2	4.8	(10.6)	10.9	15.0
Other Services	4.4	(3.4)	4.4	(2.6)	29.5
Retail Trade	(53.6)	45.6	(2.9)	(1.0)	17.7
Leisure & Hospitality	(19.4)	(2.9)	0.7	3.2	18.3
Construction	(25.2)	8.4	(6.0)	30.8	(17.1)
Transport & Utilities	(9.8)	36.9	(17.8)	21.7	(3.6)

Note: Some NAICS sectors are grouped with others. For sector definitions, see Appendix A.
Sources: NYS Department of Labor, QCEW; NYS Ways and Means Committee staff estimates.

Besides being the largest source of variable wages, the growth rate of variable wages in the securities industry is more volatile than most other sectors. The growth of variable wages in the education and health sector has been among the most consistent, with this sector being the only one to have positive variable wage growth in each of the last four years.

The Assembly Ways and Means Committee staff estimates that State total variable compensation, which was \$39.0 billion in 2004, increased by 13.9 percent to \$44.4 billion for 2005. This will be followed by growth of 15.9 percent year-over-year during 2006 and 8.9 percent in 2007 (see Figure 57).

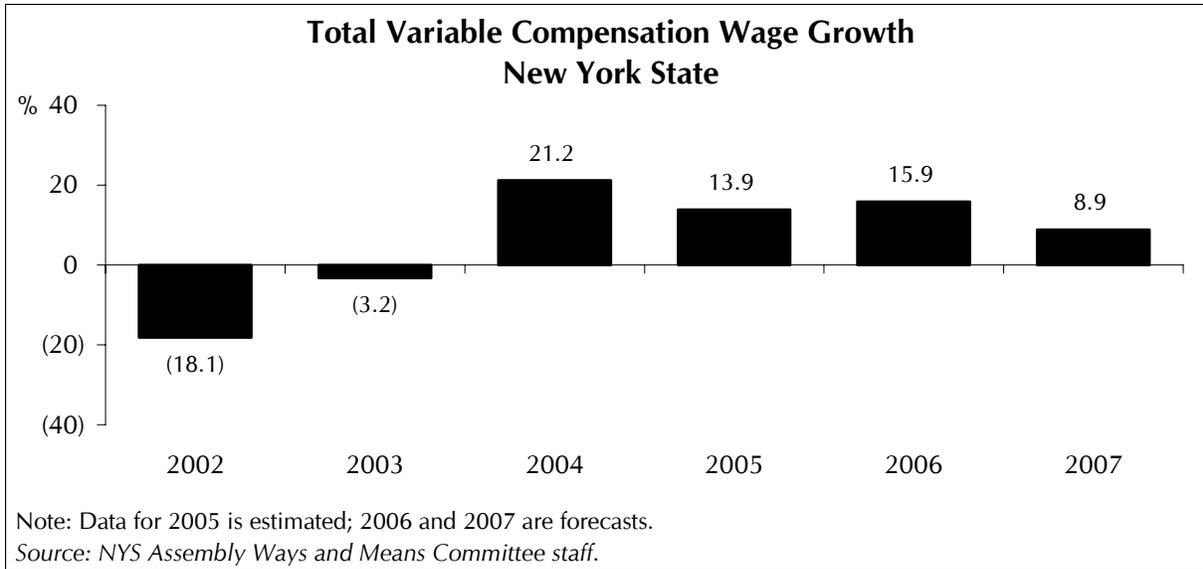


Figure 57

Variable compensation will grow faster than total wages over this period and will make up 11.6 percent of total wages by 2007. Securities industry variable compensation is expected to grow faster than other industries in 2006 and 2007 (see Figure 58).

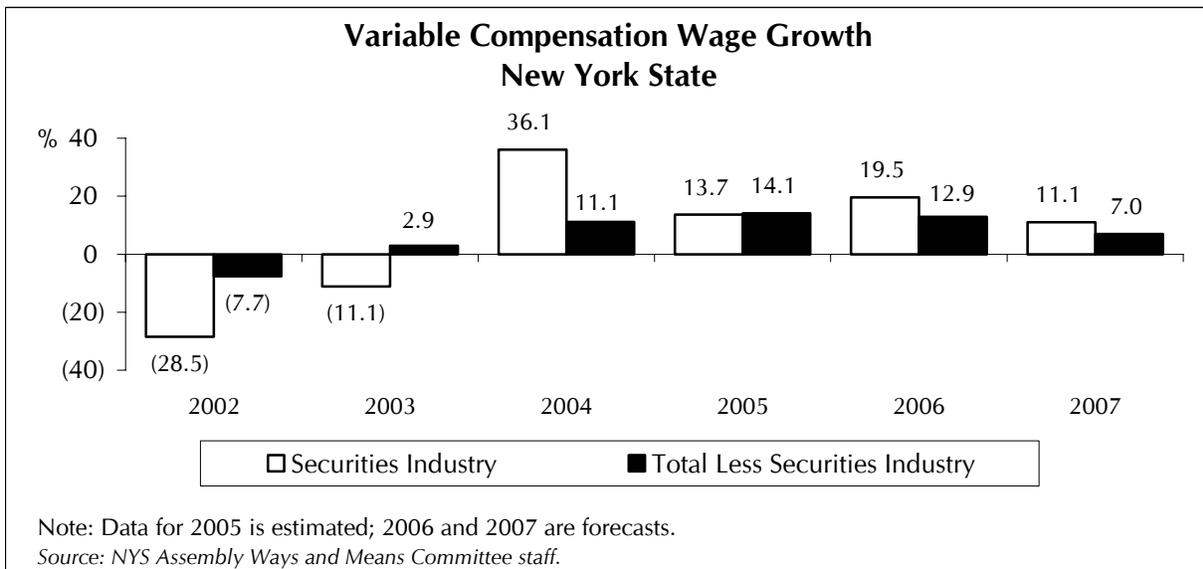


Figure 58

Securities industry variable compensation is linked with both securities industry revenue and profits. Although the stock market is not booming, it is no longer in decline, and pent-up demand for investment banking services may help to drive revenue higher in 2006 and 2007 (see Figure 59).

While Wall Street bonuses overall are expected to rise, there is always considerable variability regarding who gets these larger bonuses. Pay of top executives, which has been rising particularly rapidly, is expected to level off or even decline.

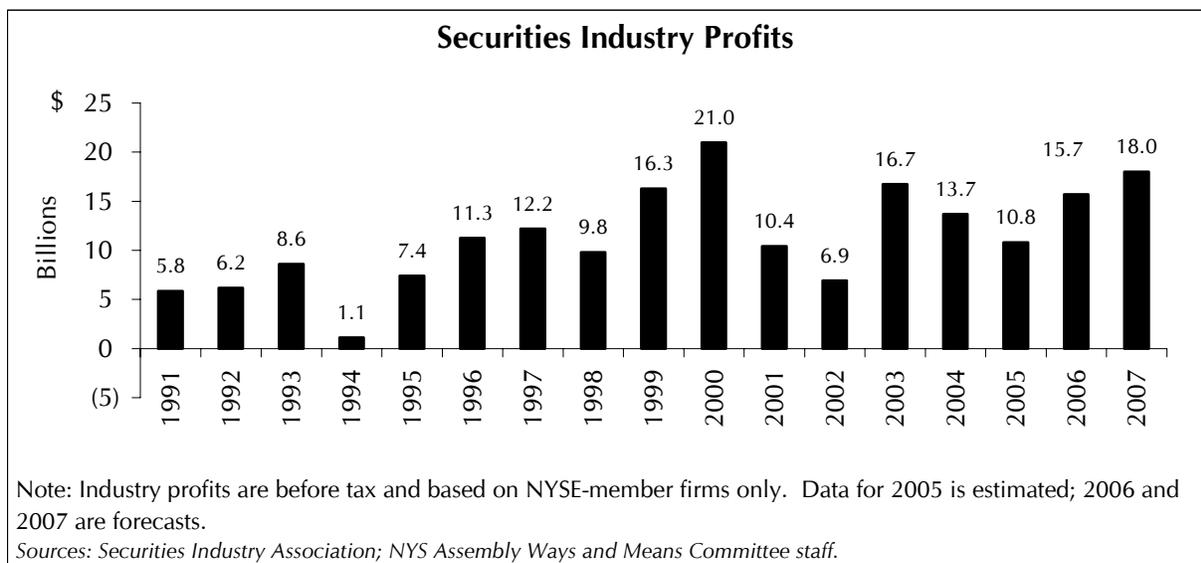


Figure 59

Financial markets and the securities industry were severely shaken by scandals and the bursting of a stock market bubble. However, both in terms of market performance and industry profitability, the worst appears to be over. Profits and revenue both peaked in 2000. Even by the end of the forecast period, profits are not expected to surpass their peak from 2000. Profit growth will be limited by price competition within the industry. In addition, changes in the way corporations involved in the securities industry account for profits have started reducing reported industry profits and will continue to do so.

Capital Gains

After rising rapidly during the booming stock market of the late 1990s, capital gains realizations plummeted in 2001 and declined further in 2002, then are estimated to have increased in 2003 and 2004 for both the State and the nation (see Figure 60). In 2005, capital gains for the nation are estimated to have grown 39.4 percent to \$703 billion, while New York State capital gains are estimated to have grown 32.3 percent to \$69 billion. This will be followed by capital gains growth of 6.4 percent to \$747 billion in 2006 for the nation and growth of 5.4 percent to \$73 billion for the State. In 2007, capital gains for the nation and State respectively are expected to grow 5.8 percent and 15.8 percent.

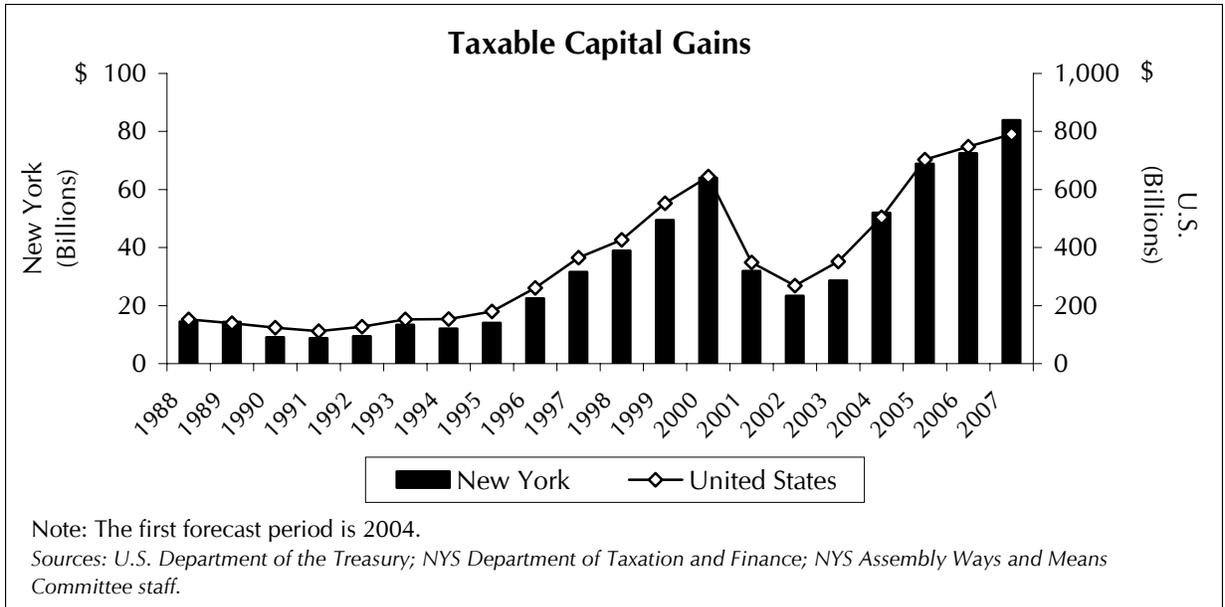


Figure 60

Traditionally, the single most important factor in driving capital gains both for the nation and New York is the performance of financial markets, particularly equity markets. However, model results indicate that it is the long-term change in equity markets rather than the year-over-year price growth that has the greatest influence on capital gains. The steep decline in stock market prices around the time of the 2001 recession are still reducing capital gains to some extent. By 2006, this will reverse and built-up stock market gains since 2002 will start to have a positive impact on capital gains. Property prices are also increasingly influencing capital gains, particularly in the recent environment of rapid price growth, increasing purchases of homes for investment purposes, and high numbers of home sales. Tax rates also affect how and when people choose to cash out their market gains, although no relevant changes in tax policy are anticipated in the forecast period.

New York State Forecast Comparison

The Assembly Ways and Means Committee staff’s employment growth forecast for 2006 is 0.9 percent (see Table 11). It is 0.2 percentage point higher than the Division of the Budget forecast and 0.1 percentage point higher than Moody’s Economy.com forecast. The Committee staff’s employment forecast for 2007 is also 0.9 percent. This is 0.2 percentage point higher than the Division of the Budget’s forecast.

Table 11

NYS Forecast Comparison (Percent Change)				
	Actual 2004	Estimate 2005	Forecast 2006	Forecast 2007
Employment				
Ways and Means	0.4	1.1	0.9	0.9
Division of the Budget	0.6	0.9	0.7	0.7
Moody's Economy.com	0.5	0.9	0.8	0.5
Wages				
Ways and Means	6.4	5.3	6.1	5.0
Division of the Budget	6.4	5.1	5.9	5.1
Moody's Economy.com	6.1	4.6	3.3	4.4
<i>Sources: NYS Assembly Ways and Means Committee staff; NYS Division of the Budget, Executive Budget 2006-07 with 30-day changes, February 2006; Moody's Economy.com, February 2006.</i>				

The Assembly Ways and Means Committee staff's wage growth forecast for 2006 is 6.1 percent. This is 2.8 percentage points higher than Moody's Economy.com forecast and 0.2 percentage point higher than the Division of the Budget's forecast.

The Ways and Means Committee staff's 2007 wage growth forecast is 5.0 percent, 0.1 percentage point lower than the Division of the Budget's forecast. It is 0.6 percentage point higher than Moody's Economy.com forecast.

RISKS TO THE FORECAST

Risks to the National Forecast

Downside Risks

Energy prices continue to represent a significant downside risk to the forecast. Unexpected events could further constrain supply, while demand continues to grow. This combined with speculation in the market makes it extremely difficult to predict crude oil prices for the near or far future. Therefore, oil prices add a large amount of uncertainty to the forecast.

Hurricanes and severe weather patterns also represent a downside risk to the national economy. Unusually strong hurricane seasons with repeated storms would be a drag on the national economy if the economies of large regions are destroyed. Also, much of the nation's energy infrastructure is located around the Gulf Coast, which is susceptible to hurricanes. Damage to oil production and gas refining capacity located on the Gulf Coast can amplify already tight supply conditions. There is some evidence that hurricanes follow a cycle, with decades of fewer smaller hurricanes on average followed by a period of larger, stronger, more frequent storms. Some evidence suggests that in 1995 the cycle entered the larger and stronger storm portion.

Interest rates present a risk to the forecast. There is a chance that the Federal Reserve will become overzealous in fighting inflation and will raise rates too far. This will hurt financial markets, which will in turn harm the economy in general. The yield curve has also become increasingly flat. Although there is reason to believe that the implications of an inverted yield curve have changed, it has historically been a good predictor of an economic downturn.

Job cuts in the auto industry will have some ripple effects on the United States economy, reducing consumption. It may also represent a bigger problem for old, large U.S. corporations, particularly in the manufacturing sector. Legacy health care and pension costs have the potential to undermine the competitive position of many more domestic companies.

Uncertainty itself can present a general risk to the forecast. Uncertainty can surround a variety of the factors taken into account for the forecast, and may be real or perceived. Many of the events or situations that create uncertainty on the part of consumers or businesses are events that have been mentioned as adding risk to the forecast in general. Among the current factors that may be contributing to a general feeling of uncertainty are the War in Iraq, the threat of another terrorist attack, and volatility in the energy market. Uncertainty may work to lower consumer confidence, and possibly consumer spending.

Terrorism remains a concern for both the national and world economy. The costs of terrorism include not only human and financial, but also the threat of attacks can be a drag on consumer confidence, and therefore consumer spending.

Upside Potential

An end to the War in Iraq would be a positive effect on the economic outlook. A decline in oil prices would also provide a positive stimulus to the economy.

Housing market activity may continue to remain resilient, helping support stronger growth in personal consumption spending as well as construction spending.

Risks to the New York State Forecast

Downside Risks

Downside risks to the national economy also present risk to the New York State economy, as the State economy would likely grow slower if there were slower national growth. Terrorism remains a concern, especially the threat of attack on State soil. Also, if the securities industry were to do worse than expected, this would negatively impact New York State wages.

Housing prices represent a risk to the national and State economies. As housing prices appreciate, there is some concern that prices may be rising too rapidly, or exceeding the price the market can bear, creating a bubble which represents a concern if it were to burst. A housing price bubble is also more risky in the current environment due to the increased use of ARMs and nontraditional mortgages. The rapid appreciation of housing prices is apparent in some regions of the State, such as Long Island; however, other regions have not experienced this phenomenon.

Energy prices represent a significant risk for the New York State economy and its consumers. Winter in the Northeast produces high heating costs for homeowners, a cost that is likely to be exacerbated by either a colder than normal winter, or rises in prices of commodities such as home heating oil.

Upside Potential

Upside potential for the national economy will also be upside potential for the State economy. Also, if the securities industry were to perform better than expected, this would help to boost New York State wages.

An unexpected improvement in energy prices presents upside potential to the forecast. Housing prices may also continue to rise rapidly, alleviating concerns about a "bubble."

APPENDIX A

The North American Industry Classification System (NAICS)

Code	NAICS Title
11	Agriculture, Forestry, Fishing and Hunting
111	Crop Production
112	Animal Production
113	Forestry and Logging
114	Fishing, Hunting and Trapping
115	Support Activities for Agriculture and Forestry
21	Mining
211	Oil and Gas Extraction
212	Mining (except Oil and Gas)
213	Support Activities for Mining
22	Utilities
221	Utilities
23	Construction
236	Construction of Buildings
237	Heavy and Civil Engineering Construction
238	Specialty Trade Contractors
31-33	Manufacturing
311	Food Manufacturing
312	Beverage and Tobacco Product Manufacturing
313	Textile Mills
314	Textile Product Mills
315	Apparel Manufacturing
316	Leather and Allied Product Manufacturing
321	Wood Product Manufacturing
322	Paper Manufacturing
323	Printing and Related Support Activities
324	Petroleum and Coal Products Manufacturing
325	Chemical Manufacturing
326	Plastics and Rubber Products Manufacturing
327	Nonmetallic Mineral Product Manufacturing
331	Primary Metal Manufacturing
332	Fabricated Metal Product Manufacturing
333	Machinery Manufacturing
334	Computer and Electronic Product Manufacturing
335	Electrical Equipment, Appliance, and Component Manufacturing
336	Transportation Equipment Manufacturing
337	Furniture and Related Product Manufacturing
339	Miscellaneous Manufacturing
42	Wholesale Trade
423	Merchant Wholesalers, Durable Goods
424	Merchant Wholesalers, Nondurable Goods
425	Wholesale Electronic Markets and Agents and Brokers

** continued on next page **

The North American Industry Classification System (NAICS) – (continued)

Code	NAICS Title
44-45	Retail Trade
441	Motor Vehicle and Parts Dealers
442	Furniture and Home Furnishings Stores
443	Electronics and Appliance Stores
444	Building Material and Garden Equipment and Supplies Dealers
445	Food and Beverage Stores
446	Health and Personal Care Stores
447	Gasoline Stations
448	Clothing and Clothing Accessories Stores
451	Sporting Goods, Hobby, Book, and Music Stores
452	General Merchandise Stores
453	Miscellaneous Store Retailers
454	Nonstore Retailers
48-49	Transportation and Warehousing
481	Air Transportation
482	Rail Transportation
483	Water Transportation
484	Truck Transportation
485	Transit and Ground Passenger Transportation
486	Pipeline Transportation
487	Scenic and Sightseeing Transportation
488	Support Activities for Transportation
491	Postal Service
492	Couriers and Messengers
493	Warehousing and Storage
51	Information
511	Publishing Industries (except Internet)
512	Motion Picture and Sound Recording Industries
515	Broadcasting (except Internet)
516	Internet Publishing and Broadcasting
517	Telecommunications
518	Internet Service Providers, Web Search Portals, and Data Processing Services
519	Other Information Services
52	Finance and Insurance
521	Monetary Authorities - Central Bank
522	Credit Intermediation and Related Activities
523	Securities, Commodity Contracts, and Other Financial Investments and Related Activities
524	Insurance Carriers and Related Activities
525	Funds, Trusts, and Other Financial Vehicles
53	Real Estate and Rental and Leasing
531	Real Estate
532	Rental and Leasing Services
533	Lessors of Nonfinancial Intangible Assets (except Copyrighted Works)
54	Professional, Scientific, and Technical Services
541	Professional, Scientific, and Technical Services

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The North American Industry Classification System (NAICS) – (continued)

Code	NAICS Title
55	Management of Companies and Enterprises
551	Management of Companies and Enterprises
56	Administrative and Support and Waste Management and Remediation Services
561	Administrative and Support Services
562	Waste Management and Remediation Services
61	Educational Services
611	Educational Services
62	Health Care and Social Assistance
621	Ambulatory Health Care Services
622	Hospitals
623	Nursing and Residential Care Facilities
624	Social Assistance
71	Arts, Entertainment, and Recreation
711	Performing Arts, Spectator Sports, and Related Industries
712	Museums, Historical Sites, and Similar Institutions
713	Amusement, Gambling, and Recreation Industries
72	Accommodation and Food Services
721	Accommodation
722	Food Services and Drinking Places
81	Other Services - except Public Administration
811	Repair and Maintenance
812	Personal and Laundry Services
813	Religious, Grantmaking, Civic, Professional, and Similar Organizations
814	Private Households
92	Public Administration
921	Executive, Legislative, and Other General Government Support
922	Justice, Public Order, and Safety Activities
923	Administration of Human Resource Programs
924	Administration of Environmental Quality Programs
925	Administration of Housing Programs, Urban Planning, and Community Development
926	Administration of Economic Programs
927	Space Research and Technology
928	National Security and International Affairs

Source: Executive Office of the President, Office of Management and Budget, North American Industry Classification System, United States, 2002.

APPENDIX B

Employment and Wages in NAICS Sectors, 2004				
	Employment (Thousands)		Wages (\$ in Billions)	
	U.S.	NYS	U.S.	NYS
Total	131,423.9	8,232.0	\$5,389.5	\$412.8
Government	21,620.4	1,397.8	927.2	65.1
Education & Health	16,951.6	1,415.4	617.6	53.3
Retail Trade	15,058.9	863.8	380.7	22.9
Other Services	13,302.2	729.9	384.7	22.9
FIRE	8,030.0	697.7	422.5	82.4
Leisure & Hospitality	12,493.1	660.1	723.3	14.9
Manufacturing	14,905.3	598.2	282.3	30.1
Professional Services	6,773.1	515.0	450.2	37.9
Wholesale Trade	5,661.5	352.7	306.2	21.3
Construction	6,974.2	320.3	292.9	15.8
Information	3,117.4	268.2	191.0	19.7
Transport & Utilities	4,811.1	256.9	385.5	11.6
Management of Companies	1,725.2	119.4	136.3	13.8
Note: Some NAICS sectors are grouped with others. For sector definitions, see Appendix A.				
<i>Sources: NYS Department of Labor, QCEW; Bureau of Labor Statistics, CES; Bureau of Economic Analysis.</i>				

APPENDIX C

U.S. Economic Outlook				
	Actual	Estimate	Forecast	Forecast
	2004	2005	2006	2007
Real GDP*	10,755.7	11,131.1	11,484.6	11,841.9
Real Consumption*	7,588.6	7,858.1	8,094.9	8,348.3
Real Investment*	1,809.9	1,915.6	2,027.5	2,096.5
Real Exports*	1,117.9	1,193.3	1,265.6	1,352.4
Real Imports*	1,719.2	1,825.2	1,923.8	2,013.2
Real Government*	1,952.3	1,985.1	2,018.1	2,055.5
<i>Federal*</i>	723.7	738.4	748.9	757.0
<i>State and Local*</i>	1,228.4	1,246.5	1,269.0	1,298.2
Personal Income**	9,713.3	10,238.2	10,867.5	11,482.1
Wages & Salaries**	5,389.5	5,711.9	6,018.0	6,336.3
Transfer Income**	1,427.5	1,525.5	1,627.1	1,747.4
Corporate Profits (Accounting Basis)**	1,059.4	1,425.8	1,529.1	1,612.5
Corporate Profits (Economic Basis)**	1,161.5	1,345.7	1,467.8	1,552.4
Productivity (1992 = 100)	132.3	135.8	139.1	142.5
Employment***	131.4	133.5	135.5	137.5
CPI-Urban (1982-84 = 100)	188.9	195.3	201.5	206.9
S&P 500 Stock Price (1941-43 = 10)	1,130.6	1,207.1	1,315.1	1,416.3
Treasury Bill Rate (3-month)****	1.4	3.2	4.6	4.7
Treasury Bond Rate (10-year)****	4.3	4.3	5.0	5.3
<p>* In billions of chained 2000 dollars. ** In billions of dollars. *** In millions. **** Annual average rate.</p> <p><i>Sources: Bureau of Economic Analysis; Bureau of Labor Statistics; Federal Reserve Board of Governors; Standard and Poor's; NYS Assembly Ways and Means Committee staff.</i></p>				